SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 128

THE TEXAS & PACIFIC RAILWAY COMPANY, PETITIONER,

vs.

S. O. POTTORFF, RECEIVER OF THE FIRST NATIONAL BANK OF EL PASO, TEXAS

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

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Caption.

Be it remembered that at a regular term of the District Court of the United States for the Western District of Texas, in the El Paso Division thereof, the Honorable Charles A. Boynton, a United States District Judge, then and there presided and held a session of said court at the City of El Paso; that said term began on the 4th day of April, 1932, and is, on this 29th day of August, 1932, still in session, and will not terminate by operation of law until the close of the 2d day of October, 1932; that during said term and session there came on to be heard on the 25th day of May, 1932, and was determined on the 26th day of May, 1932, the following cause:

The Texas and Pacific Railway Company

vs.

S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas.

No. 251 in Equity.

A transcript of the proceedings follows:

In the District Court of the United States for the Western District of Texas, El Paso Division.

THE TEXAS AND PACIFIC)
RAILWAY COMPANY,)
Plaintiff,)
vs.)No. 251 IN EQUITY.
S. O. POTTORFF, RECEIVER)
OF THE FIRST NATIONAL)
BANK OF EL PASO, TEXAS,)
Defendant.)

AMENDED BILL OF COMPLAINT.

To the Honorable Judge of Said Court:

Comes now The Texas and Pacific Railway Company, plaintiff in the above entitled and numbered cause, and by leave of the Court files this its First Amended Bill of Complaint in lieu of its Original Bill of Complaint filed herein on March 1, 1932, complaining of S. O. Pottorff, Receiver of The First National Bank of El Paso, defendant, respectfully represents:

I

1. Plaintiff, The Texas and Pacific Railway Company, is a corporation duly chartered and organized and now existing under and by virtue of the laws of the United States, to-wit: An Act of Congress entitled "An Act to incorporate the Texas Pacific Railroad Company, and to aid in the construction of its road, and for other purposes," approved March 3, 1871, and Acts amendatory thereof and supplemental thereto, including an Act of Congress approved May 2, 1872, whereby, among other things, the name, style and title of said Texas Pa-

cific Railroad Company was changed to "The Texas and Pacific Railway Company." Plaintiff has its principal office and place of business at Dallas in Dallas County in the Dallas Division of the Northern District of Texas.

2. Defendant, S. O. Pottorff, Receiver of The First National Bank of El Paso, is the duly appointed, qualified and acting Receiver of said bank, an insolvent national banking association, and is now residing and acting as such Receiver in El Paso County in the El Paso Division of the Western District of Texas.

II

This is a suit in equity over which the District Court of the United States for the Western District of Texas, El Paso Division, is given original jurisdiction by Section 41, paragraphs 1 and 16, Title 28, and by Section 94, Title 12, of the Code of Laws of the United States, as revised and enacted by Congress on June 28, 1926, and approved on June 30, 1926.

III

1. That heretofore, to-wit, on the 3rd day of July, 1922, while the Texas and Pacific Railway was being operated by J. L. Lancaster and Charles L. Wallace, Receivers appointed by the District Court of the United States in and for the Western District of Louisiana, Monroe Division, and upon their petition, an order was made and entered by said Court authorizing said Receivers to select The First National Bank of El Paso as an additional depository for receivership funds, which order among other things provided that said bank "shall be required to furnish bond with good and solvent sureties, * * * * in such an amount as will substantially equal the estimated average daily balances to be carried by said

Receivers in said bank." A copy of said petition and order is attached hereto, marked "Exhibit A," and made a part hereof.

2. That thereafter, on or about July 10, 1922, The First National Bank of El Paso, as principal, and National Surety Company, as surety, executed and delivered to said Receivers their certain surety bond for the sum of $25,000.00, conditioned as required by said order of said Court and payable to said Receivers, for the purpose of securing the repayment of deposits made by them in said bank upon their demand, and said Receivers thereupon opened an account with said bank and made deposits therein approximately in the amount of said surety bond.

3. That said receivership of The Texas and Pacific Railway Company was terminated on or about May 14, 1924, and, upon the written request of plaintiff, said The First National Bank of El Paso, as principal, and National Surety Company, as surety, executed and delivered to The Texas and Pacific Railway Company on or about August 7, 1924, a new surety bond in the sum of $25,000.00, payable to said railway company, guaranteeing repayment of monies deposited to its credit in said bank in the manner provided in said bond, a copy of which is attached hereto, marked "Exhibit B," and made a part hereof

4. That thereafter, during the month of April, 1927, the amount of plaintiff's deposits in said bank increased to such extent as to require additional security, and upon the written request of plaintiff said The First National Bank of El Paso, as principal, and Maryland Casualty Company, as surety, executed and delivered to The Texas and Pacific Railway Company on or about April 25, 1927, an additional surety bond in the sum of $25,-

000.00, payable to said railway company, guaranteeing repayment of monies deposited to its credit in said bank in the manner provided in said bond, a copy of which is attached hereto, marked "Exhibit C," and made a part hereof.

IV

1. During the month of January, 1931, while said The First National Bank of El Paso was solvent and a going concern, and while said surety bonds guaranteeing payment to plaintiff of plaintiff's said deposits in said bank were in full force and effect, the duly authorized officers of said bank represented to the officers of The Texas and Pacific Railway Company that said bank was required to pay heavy yearly premiums upon said surety bonds, and that said bank could effect the saving of such premiums by substituting United States Liberty bonds for said surety bonds for the securing of such deposits; that said bank could lawfully make such substitution and was so advised by its attorneys; that said bank desired to discontinue payment of such premiums on such surety bonds and in lieu thereof to pledge United States Liberty bonds of the value of $50,000.00 to secure the repayment of monies deposited by said railway company in said bank; and said The Texas and Pacific Railway Company, relying upon the representations so made by the officers of said bank that the pledge of said liberty bonds would be legal and valid and would constitute and be a binding and enforcible obligation against said bank, agreed to such substitution of said securities in lieu of said surety bonds to secure payment of said deposit, and except for said agreement on the part of defendant to substitute said liberty bonds for said surety company's guaranties plaintiff would have withdrawn its said deposit from said bank, unless such

surety bonds had been continued in full force and effect at the cost and expense of said bank.

2. That thereafter on or about January 29, 1931, the duly authorized officers of said The First National Bank of El Paso, with the full knowledge and approval of its Board of Directors, and pursuant to said substitution agreement, in good faith and in the regular course of its business, placed its certain seven (7) United States Government Fourth Liberty Loan 4¼ Coupon Bonds 1933-38, of the aggregate amount and value of $50,000.00, described by numbers and amounts, as follows:

G00129907	$ 5,000.00
A00115901	$ 5,000.00
E00040105	$ 5,000.00
K00129870	$ 5,000.00
G00353057	$10,000.00
H00353058	$10,000.00
H00298068	$10,000.00

in its Trust Department and with its Trust Officer in a separate envelope bearing the name of said railway company to be held, and were held separate and apart from all other securities of said bank, in trust for the use and benefit of said The Texas and Pacific Railway Company for the purpose of protecting it against any loss that it might sustain by reason of continuing to maintain its said deposits in said bank and for the purpose of guaranteeing the repayment of said deposits in full to said railway company upon its demand; and that there was deposited with said liberty bonds a certain pledge agreement prepared by the attorneys for said bank executed on January 29, 1931, by said The First National Bank of El Paso, acting by and through F. M. Murchison, its president, and J. E. Benton its cashier, thereunto duly authorized, with the full knowledge and

approval of the Board of Directors of said bank, a copy of which agreement is attached hereto, marked "Exhibit D," and made a part hereof. Thereupon, said surety bonds were cancelled as of January 30, 1931, and plaintiff thereafter relied upon said liberty bonds so pledged by said agreement of said The First National Bank of El Paso as security for the repayment of all monies to its credit in said bank; that said bank, its depositors, creditors and stockholders were benefitted by the substitution of said liberty bonds for said surety bonds in the amount of the premiums saved on the latter, and were benefitted in the increase of its assets by reason of said deposit, and the interest earned by said bank thereon; and the placing of said liberty bonds by said bank to secure plaintiff's said deposits was necessarily incident to the carrying on of the business of said bank, and in the receiving and retention of said deposit.

V

1. That thereafter said The Texas and Pacific Railway Company continued to have deposits in said The First National Bank of El Paso and maintained an average daily balance in said bank in excess of $50,000.00; that said bank thereafter continued to accept and pay plaintiff's drafts and checks drawn against its said deposits until on or about September 4, 1931, when said bank failed, became insolvent, closed its doors to the public and refused to accept, honor or pay any other or further checks or drafts drawn by plaintiff against said deposits; that said The Texas and Pacific Railway Company had on deposit in said bank on September 4, 1931, the sum of $54,646.94, including accrued interest, which sum of money it was entitled to receive from said bank upon demand, and that by reason thereof said The First

National Bank of El Paso, at the time of its failure, was indebted to plaintiff in said amount,

2. That thereafter, on or about September 6, 1931, the Comptroller of the Currency of the United States duly and regularly appointed S. O. Pottorff receiver of said The First National Bank of El Paso, and said receiver, on or about September 8, 1931, took charge of all the affairs, assets and securities of said bank, including plaintiff's said deposits, and said Receiver on said date also took possession of the Trust Department of said bank in which said liberty bonds were held as security for the repayment of the monies of said railway company on deposit in said bank, as aforesaid, and said Receiver has ever since said date held said bonds, and now wrongfully holds the same in his possession, and by reason thereof said Receiver became indebted and is now indebted to plaintiff in the sum of $54,646.94 plus interest thereon at the rate of six per cent per annum from September 4, 1931.

3. That thereafter, on or about November 7, 1931, said The Texas and Pacific Railway Company, acting by and through its duly authorized officers and agents, filed with said Receiver its claim against said bank as a secured creditor for the sum of $54,646.94; that said Receiver admitted the correctness of the amount of said claim but denied that it was secured by said liberty bonds and refused to recognize said agreement made by said bank as aforesaid, and to allow plaintiff's claim for the full amount thereof as he is bound to do under and by virtue of said pledge agreement, but on the contrary said Receiver wrongfully and unlawfully denies to plaintiff its right to have said liberty bonds rendered subject to said pledge agreement and wrongfully and unlawfully withholds said bonds and seeks to appropriate the value

thereof to the use and benefit of the general creditos of said bank.

VI

1. That said the First National Bank of El Paso is hopelessly insolvent and said Receiver is unable to pay the unsecured depositors of said bank more than thirty per cent of the amount of their deposits, and unless said liberty bonds or the proceeds from the sale thereof are applied to plaintiff's said claim in accordance with said agreement it will sustain irreparable loss and injury.

2. Said liberty bonds, at the time they were deposited with the Trust Department of said bank on or about January 29, 1931, as aforesaid, had a reasonable market value of $50,000.00, but that the present reasonable market value of said liberty bonds is not in excess of $45,000.00.

VII

1. That said liberty bonds are now in possession of and on deposit with said Receiver for the purpose of protecting plaintiff against any loss that it might sustain by reason of its said deposits in said bank and as a guarantee for the repayment of said deposits to plaintiff upon its demand, and there now exists and at all times since January 29, 1931, there has existed, a lien upon and against said liberty bonds in favor of plaintiff to secure the repayment of the full amount of its deposits as aforesaid.

2. That said Receiver has neither the right nor the authority to use or devote said liberty bonds or the proceeds arising from the sale thereof to any purpose other or different from that expressed in said agreement, but plaintiff is informed and believes and therefore avers

that said Receiver has intended and now intends to treat said liberty bonds or the proceeds arising from the sale thereof as general assets of said bank for the use and benefit of all its creditors.

3. That plaintiff is entitled, at its option, either to have said Receiver deliver said liberty bonds to it and to credit its said claim with the market value thereof at the time of said delivery, or to have said Receiver sell said liberty bonds at the highest obtainable price and apply the proceeds of the sale thereof to its claim against said bank.

4. That plaintiff has demanded of said Receiver that he deliver said liberty bonds to it and credit its said claim with the market value thereof at the time of said delivery but said Receiver has failed and refused and still refuses so to do; and upon such refusal, plaintiff demanded of said Receiver that he sell said liberty bonds and apply the proceeds from the sale thereof to its said claim in accordance with said agreement but said Receiver has failed and refused and still refuses so to do.

VIII

1. That said The First National Bank of El Paso was authorized and empowered as a national banking association to make said agreement and to deposit said liberty bonds for the purpose and in the manner aforesaid, and when said liberty bonds were so deposited they became, in the event of default by said bank, primarily liable for any loss plaintiff might sustain by reason of said deposits.

2. That at the time of the execution of said agreement and the deposit of said liberty bonds and at all times thereafter, said The First National Bank of El

Paso was operated under the direction and control of the Comptroller of the Currency of the United States, and said Comptroller was under the duty to promulgate such rules and regulations concerning the practice of said bank with reference to receiving and securing deposits and to disapprove any act of said bank not in accordance with the lawful powers of such bank; that said Comptroller did not at any time after said bank had pledged said bonds to secure said deposit make any complaint to said bank or in any manner object to the said pledge agreement on the part of said bank, but permitted said bank and the duly authorized examiners of said bank, after said Comptroller had obtained full knowledge of said agreement, to continue to receive deposits from plaintiff in accordance with said pledge agreement and to enjoy the benefits of such deposits, and said Receiver may not now, after the default of said bank and its failure to repay said deposits upon plaintiff's demand, repudiate or otherwise question the validity of said agreement and the pledge of said bonds without refunding to plaintiff the full amount of its said deposit in said bank at the time it ceased to do business.

IX

Plaintiff alleges and shows to the court that if it should be held that the pledge agreement hereinbefore alleged is uninforcible, then plaintiff alleges that it is entitled to have said Receiver return to it the full amount of its money on deposit in such bank on September 4, 1931 with lawful interest thereon from said date as for money had and received by said bank, which in equity and good conscience, under the facts and circumstances, it is bound to return to plaintiff.

WHEREFORE, and for as much as plaintiff has not

an adequate remedy at law, and is entitled to relief under the principles administered in Courts of Equity where matters of this nature are properly cognizable, plaintiff prays:

1. That writ of subpoena issue out of and under the seal of this court, directed to the defendant, S. O. Pottorff, Receiver of The First National Bank of El Paso, requiring him to appear on a day set before this court and then and there full, true and correct answers make to all and singular the allegations herein, but not under oath, answer under oath being expressly waived, and to perform and abide by such orders, directions and decrees as may be entered herein; and

2. That upon hearing hereof the Court by its decree adjudge that The Texas and Pacific Railway Company is a secured creditor of The First National Bank of El Paso to the amount or value of said liberty bonds; that said bonds are held by said Receiver in trust for the use and benefit of plaintiff for the purpose of protecting it against any loss that it might sustain by reason of its said deposits in said bank and as a guarantee for the repayment of said deposits upon its demand; that an equitable lien exists upon and against said bonds for said purposes in favor of The Texas and Pacific Railway Company; and

3. That the Court by its decree direct and order defendant, S. O. Pottorff, Receiver of The First National Bank of El Paso, to forthwith deliver said liberty bonds to The Texas and Pacific Railway Company and to credit its said claim with a sum equal to the current market price of said bonds in El Paso on the date of said delivery; and

4. That the Court by its decree further adjudge that

said liberty bonds when so delivered to plaintiff by said Receiver shall become the sole and separate property of The Texas and Pacific Railway Company; and

5. In the alternative and in the event the Court should hold that complainant is not entitled to the possession of said bonds and does not have the right to sell or otherwise dispose of the same, complainant prays that the Court by its decree direct and order said Receiver to sell said liberty bonds forthwith at the highest obtainable price, to deliver the proceeds thereof to The Texas and Pacific Railway Company, and to credit its said claim of $54,646.94, with lawful interest thereon from September 4, 1931, with said sum of money; and

6. That the court by its decree further adjudge that the relief prayed for and granted herein is without prejudice to the right of complainant to recover of and from said Receiver any other or further sum or sums of money owing to it by said Receiver after said bonds or the proceeds from the sale thereof are charged against its said claim;

7. Or, in the alternative, if the court should hold that plaintiff cannot recover as prayed for upon its pledge agreement, then in such event plaintiff prays that it be ordered and decreed by the court that defendant return to plaintiff the full amount of its deposit, to-wit, the sum of $54,646.94, with interest thereon as aforesaid, as for money had and received;

8. That complainant have such other and further relief in the premises, including all costs of court, as the nature and circumstances of this suit may require, and as the court may deem just and proper.

Respectfully submitted,

S. N. RUSSELL,
D. W. HARRINGTON,
M. E. CLINTON,
T. D. GRESHAM,
Attorneys for Plaintiff, The Texas and Pacific Railway Company.

In the District Court of the United States in and for the Western District of Louisiana, Monroe Division.

B. F. BUSH, Receiver of the railroads, etc., of St. Louis, Iron Mountain & Southern Railway Company, *Complaniant,*	)
against	) No. 1120 In Equity.
THE TEXAS AND PACIFIC RAILWAY COMPANY, *Defendant.*	)

To the Honarable, Rufus E. Foster, Judge of said Court:

The petition of J. L. Lancaster and Charles L. Wallace, Receivers herein, would respectfully represent that by an order made herein on the 4th day of November, 1916, certain banks located at various points along the line of road in charge of your Receivers were designated as depositories of the funds of the Receivers.

Your petitioners would state that El Paso, Texas, is at the extreme Western Termini of the line of road in their charge, and that the State National Bank of El Paso was designated depository by the order of Novemvember 4, 1916.

Your petitoners would respectfully state that, in their opinion, an additional depository should be had at El Paso, and that it is to the interest of your Receivers to have the Court designate the First National Bank of El

Paso as a bank in which your Receivers are authorized to deposit their funds.

The said First National Bank of El Paso, is the largest bank in El Paso, is solvent in every way, and is in a condition to be of service to your Receivers in many ways.

That said bank will comply with the order of Court applying to other depositories and will give bond to protect your Receivers against any loss.

J. L. LANCASTER and CHARLES L. WALLACE
Receivers of
THE TEXAS AND PACIFIC RAILWAY COMPANY.

(Signed) By THOMAS J. FREEMAN
General Counsel for Receivers.

EXHIBIT A.

ORDER

Upon the filing and reading of the foregoing petition, and upon consideration thereof, it is ordered that the Receivers herein are authorized to select as an additional depository of the funds of the Receivers, the First National Bank of El Paso, Texas.

That said First National Bank of El Paso, Texas, shall be required to furnish bond with good and solvent sureties, (either corporation or individual) in such an amount as will substantially equal the estimated average daily balances to be carried by said Receivers in said bank.

Thus done and signed, this the 3rd day of July 1922.

(Signed) RUFUS E. FOSTER
United States District Judge.

Filed July 6, 1922,
W. B. Lee, Clerk,
U. S. Dist. Court,
West. Dist. of Louisiana.

EXHIBIT A.

THE STATE OF TEXAS)
COUNTY OF EL PASO.)

KNOW ALL MEN BY THESE PRESENTS, That We, The First National Bank of El Paso, Texas, as principals, and The National Surety Company of New York, as surety, acknowledge to owe and be indebted jointly, severally and in solido to The Texas and Pacific Railway Company, in the sum of TWENTY-FIVE THOUSAND DOLLARS ($25,000.00) for the payment of which well and truly to be made, we hereby bind ourselves, our successors, assigns and legal representatives jointly, severally and in solido.

IN WITNESS WHEREOF we have hereunto set our hands at El Paso, Texas, this 7th day of August, A. D. 1924.

But the above obligation is subject to the following condition: That if the said The First National Bank of El Paso, Texas, shall well and truly, on demand, pay over and deliver to The Texas and Pacific Railway Company, or its order, all and such sums of money, funds and valuables, general and special, as may now be on deposit by, in favor of, or in the name of The Texas and Pacific Railway Company with the said The First National Bank of El Paso, Texas, and as may be deposited hereafter by The Texas and Pacific Railway Company or by any one for its account, with the said The First National Bank of El Paso, Texas, or that may come into the custody or control of said The First National Bank

of El Paso, Texas, for account of The Texas and Pacific Railway Company, then and in that event the above obligation shall become null and void; otherwise to remain in full force and effect.

In event it becomes necessary to enforce the obligation of this bond by suit, all costs of same, including attorney's fees, are to be paid by the principals and surety herein.

FIRST NATIONAL BANK OF EL PASO, TEXAS
By JAMES G. McNARY
President

ATTEST:
(Signed) J. E. BENTON
Cashier.
(SEAL)

NATIONAL SURETY COMPANY, Surety.
By A. M. CLARK
Vice President, Surety

ATTEST:
A. C. MILLIKAN,
Asst. Secretary.
(SEAL)

EXHIBIT B.

MARYLAND CASUALTY COMPANY
BALTIMORE

DEPOSITORY BOND

STATE OF TEXAS)
COUNTY OF EL PASO)

NOW ALL MEN BY THESE PRESENTS:

That we, The First National Bank of El Paso, Texas,

as principals, and MARYLAND CASUALTY COMPANY of Baltimore, Maryland, as surety, acknowledge to owe and be indebted jointly, severally and in solido to The Texas and Pacific Railway Company, in the sum of TWENTY FIVE THOUSAND DOLLARS ($25,000.00), for the payment of which well and truly to be made, we hereby bind ourselves, our successors, assigns and legal representatives jointly, severally and in solido.

IN WITNESS WHEREOF we have hereunto set our hands at El Paso, Texas, this 25th day of April, A. D. 1927.

But the above obligation is subject to the following condition: That if the said The First National Bank of El Paso, Texas, shall well and truly, on demand, pay over and deliver to The Texas and Pacific Railway Company, or its order, all and such sums of money, funds and valuables, general and special, as may now be on deposit by, in favor of, or in the name of The Texas and Pacific Railway Company with the said The First National Bank of El Paso, Texas, and as may be deposited hereafter by The Texas and Pacific Railway Company or by any one for its account, with the said The First National Bank of El Paso, Texas, or that may come into the custody or control of said The First National Bank of El Paso, Texas, for account of The Texas and Pacific Railway Company, then and in that event the above obligation shall become null and void; otherwise to remain in full force and effect.

In event it becomes necessary to enforce the obligation of this bond by suit, all costs of same, including attorney's fees, are to be paid by the principals and surety herein.

The Surety shall have the right to terminate its suretyship under this obligation by serving notice, in writing, of its election so to do, upon said The Texas and Pa-

cific Railway Company, or its lawful representatives, and thereupon the said Surety shall be discharged from any and all liability hereunder for any default of the Principal occurring after the expiration of thirty (30) days after the service of such notice.

WITNESS OUR HANDS AND SEALS.

FIRST NATIONAL BANK OF EL PASO
By F. M. MURCHISON
Vice President

ATTEST:
J. E. BENTON
Cashier.
(SEAL)

MARYLAND CASUALTY COMPANY
Surety
By HERMAN A. TAYLOR
Attorney-in-Fact.

(SEAL)

EXHIBIT C.

STATE OF TEXAS)
COUNTY OF EL PASO.)

THIS INSTRUMENT WITNESSETH:

The Texas and Pacific Railway Company, a corporation, carries an open checking account with the undersigned, The First National Bank of El Paso, in El Paso, Texas, and desires to continue so to do, and the Bank desires to continue to hold the said deposit.

For the purpose of securing the said Texas & Pacific Railway Company against any loss that might possibly occur by reason of its continuance and maintenance of the said deposit, The First National Bank of El Paso

has on this date deposited in its Trust Department, and with its Trust Officer which fact is evidenced by the signed statement to that effect of the said Trust Officer hereto attached, United States Government Liberty Bonds of the par value of Fifty Thousand ($50,000.00) Dollars, to be held by the said Trust Department, through its Trust Officer, in trust for the use and benefit of the said Texas & Pacific Railway Company. This is for the purpose of protecting it against loss as aforesaid, and it is agreed that the said Bonds shall, at all times, remain in the Trust Department as such security. Provided, however, that should the Bank at any time desire to withdraw the Liberty Bonds herewith deposited, and substitute therefor other bonds of the United States of America, or Treasury Receipts of the Treasury Department of the United States of America of equal par value, it shall have the right so to do.

Upon the closing of the said account, and only then, shall the said The First National Bank of El Paso have the right to withdraw the said securities from its Trust Department.

IN WITNESS WHEREOF, the said The First National Bank of El Paso has caused this instrument to be executed in duplicate by its President, attested by its Cashier or Assistant Cashier, and its corporate seal hereunto affixed, at El Paso, Texas, this 29th day of January, 1931, one copy being delivered to The Texas and Pacific Railway Company and one copy deposited with the Bonds with the Trust Department.

THE FIRST NATIONAL BANK OF EL PASO
(Signed) F. M. MURCHISON
President.

ATTEST:
(Signed) J. E. BENTON, Cashier,
(Seal of The First National Bank of El Paso)

STATE OF TEXAS)
COUNTY OF EL PASO.)

I, H. W. Moore, Trust Officer of The First National Bank of El Paso, hereby acknowledge receipt of the Trust Department of the said Bank of the Bonds above named and upon the conditions therein set forth.

(Signed) H. W. MOORE,
Trust Officer,
The First National Bank of El Paso.

EXHIBIT D.

Filed May 25, 1932. D. H. Hart, Clerk, By J. N. Phillips, Deputy Clerk.

Motion to Dismiss Amended Bill of Complaint.

To the Honorable Charles A. Boynton, Judge of the United States District Court for the Western District of Texas:

Now comes S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, Respondent in the above cause, and moves the Court to dismiss the Amended Bill of Complaint filed in this cause because said Bill does not state any matter of equity entitling Complainant to the relief prayed for, nor are the facts, as stated, sufficient to entitle Complainant to any relief against this Respondent.

WHEREFORE, this Respondent prays the Judgment of this Court whether he shall further answer, and that he be dismissed with his costs.

A. H. GOLDSTEIN
JONES, GOLDSTEIN, HARDIE & GRAMBLING

T. HARDIE

Solicitors for the Respondent.

Filed May 25, 1932. D. H. Hart, Clerk, By J. N. Phillips, Deputy Clerk.

Cross Bill of S. O. Pottorff, Receiver.

To the Honorable Charles A. Boynton, Judge of the United States District Court for the Western District of Texas:

Comes now S. O. Pottorff, Receiver of the First National Bank of El Paso, Texas, hereinafter styled Cross Complainant, and by leave of the Court, files this, his original Cross Bill, complaining of The Texas and Pacific Railway Company, hereinafter styled Cross Respondent, and so represents to the Court:

I.

Cross Complainant is the duly appointed, duly qualified and acting receiver of The First National Bank of El Paso, Texas, an insolvent national banking association, duly incorporated under the laws of these United States of America, and the said S. O. Pottorff, in his official capacity, is now residing in and is acting as Receiver in El Paso County, in the El Paso Division of the Western District of Texas, where said banking corporation had its office and place of business.

II.

The Cross Respondent is a corporation duly incorporated under and by virtue of the laws of the United States, to-wit, under and by virtue of an act of Congress, entitled "An Act to Incorporate The Texas Pacific Railroad Company and to Aid in the Construction of its Road

and for Other Purposes," approved March 3, 1871, and Acts amendatory thereof and supplementary thereto, including an Act of Congress approved May 2, 1872, whereby, among other things, the name and style and title of said Texas Pacific Railroad Company was changed to "The Texas and Pacific Railway Company," and Cross Respondent has its principal office and place of business in Dallas County, in the State of Texas.

III.

On or about the 29th of January, 1931, Cross Respondent demanded of The First National Bank of El Paso, Texas, that it give security to guarantee the payment by said Bank to the Cross Respondent of any deposits that might be made by the Cross Respondent in said Bank, and, in order to comply with said demand, The First National Bank of El Paso, Texas, executed and delivered to the Cross Respondent a certain instrument in writing, having the terms and provisions as set forth in Exhibit "A," hereto attached, and in connection with said Agreement, said Bank pledged its certain seven (7) United States government Fourth Liberty Loan 4¼% coupon bonds, 1933-1938, of the aggregate amount and value of $50,000.00, described by numbers and amounts as follows:

G00129907	$ 5,000.00
A00115901	5,000.00
E00040105	5,000.00
K00129870	5,000.00
G00353057	10,000.00
H00353058	10,000.00
H00298068	10,000.00

all of them constituting and being assets of The First National Bank of El Paso, Texas, and in which the general

funds of said Bank had been invested, and deposited same in its Trust Department, and with its Trust Officer, to be held separate and apart from the other securities of said Bank, under and in accordance with the terms and provisions of the Contract mentioned and referred to and described in "Exhibit A," and all of said Bonds remained so in the possession of The First National Bank of El Paso, Texas, up to the time that Cross Complainant qualified as Receiver of The First National Bank of El Paso, Texas.

IV.

At the time the Agreement referred to as Exhibit "A" was executed, and at the time the Liberty Bonds were placd in the Trust Department as above alleged, Cross Respondent had certain funds on deposit with The First National Bank of El Paso, Texas, and The First National Bank of El Paso, Texas, was indebted to Cross Respondent for funds so deposited; and, thereafter, from time to time, the Cross Respondent deposited additional sums and made withdrawals of funds from time to time from said Bank. The Cross Respondent, on September 4, 1931, the date upon which said Bank became insolvent and closed its doors, and also on September 6, 1931, the date upon which the Comptroller of the Currency of the United States duly and regularly appointed S. O. Pottorff Receiver of The First National Bank, and also on September 8, 1931, the date upon which said Receiver qualified and took charge of all of the assets and securities and affairs of said Bank, had on deposit with said Bank and standing to its credit on the books of said Bank, the sum of $54,336.74, payable to the Cross Respondent on demand, and said amount included accrued interest on the deposit balances theretofore maintained by the Cross Respondent in said Bank, and in addition to such

liability, The First National Bank of El Paso, Texas, and S. O. Pottorff, Receiver of said Bank, were, on the dates above mentioned, indebted to Cross Respondent in an additional sum of $310.20, as evidenced by a Cashier's Check which had theretofore been issued by The First National Bank of El Paso, Texas, to Cross Respondent, and which was payable to Cross Respondent and held by Cross Respondent, and which, although duly presented to said Bank, has never been paid.

V.

The assets which Cross Complainant received as Receiver of The First National Bank of El Paso, Texas, are not sufficient to pay the general creditors of said Bank the full amount of their claims, and Cross Respondent is asserting a lien upon the Liberty Bonds hereinabove set forth.

VI.

The officers of The First National Bank of El Paso, Texas, had no right or authority to make any such agreement as they attempted to make, and the terms of which are set forth in Exhibit "A," and said Bank was without authority to make said Agreement. Any such Agreement was and is ultra vires, contrary to public policy, contrary to the Statutes of the United States, and is absolutely void and of no force and effect, and the enforcement of any such Agreement would be in fraud of the rights of the general unsecured depositors of The First National Bank of El Paso, Texas, whose rights are represented by Cross Complainant, by the claims which are being asserted by the Cross Respondent casting a cloud upon the title of Cross Complainant to said Liberty Bonds and interfering with the sale of said bonds by Cross Complainant, and it is necessary that said bonds

be sold and disposed of by him in order that he may properly administer and pay out the assets of The First National Bank of El Paso, Texas, to those persons entitled to receive the proceeds of said assets, including the general depositors of said Bank. The reasonable market value of the Liberty Bonds above referred to has declined since Cross Complainant was appointed and qualified as Receiver of said Bank, and the market value of such Bonds will probably continue to decline.

WHEREFORE, PREMISES CONSIDERED, Cross Complainant prays the Court to enter an Order adjudging and decreeing that the Contract, a copy of which is hereto attached and market Exhibit "A," was and is void and of no force and effect, and that the Liberty Bonds hereinabove described are part of the general assets of The First National Bank of El Paso, Texas, which passed to and became the property of Cross Complainant, and constitute assets to be administered by him for the benefit of the general creditors and depositors of The First National Bank of El Paso, Texas, and your Cross Complainant prays for an Order decreeing that the Cross Respondent has no right, title, interest or claim in said Liberty Bonds, and your Cross Complainant prays for an Order enjoining and restraining the Cross Respondent from asserting any further rights or claims in said Liberty Bonds, and your Cross Respondent prays for such other and further relief as in equity he may be entitled to have and receive under the allegations of this Cross Bill.

A. H. GOLDSTEIN
JONES, GOLDSTEIN, HARDIE & GRAMBLING
T. HARDIE
Solicitors for Cross Complainant.

EXHIBIT "A."

STATE OF TEXAS,)
COUNTY OF EL PASO.)

THIS INSTRUMENT WITNESSETH:

The Texas & Pacific Railway Company, a corporation, carries an open checking account with the undersigned, The First National Bank of El Paso, in El Paso, Texas, and desires to continue so to do, and the Bank desires to continue to hold the said deposit.

For the purpose of securing the said Texas & Pacific Railway Company against any loss that might possibly occur by reason of its continuance and maintenance of the said deposit, The First National Bank of El Paso has on this date deposited in its Trust Department, and with its Trust Officer, which fact is evidence by signed statement to that effect of the said Trust Officer hereto attached, United States Government Liberty Bonds of the par value of Fifty Thousand ($50,000.00) Dollars, to be held by the said Trust Department, through its Trust Officer, in trust for the use and benefit of the said Texas & Pacific Railway Company. This is for the purpose of protecting it against loss as aforesaid, and it is agreed that the said Bonds shall, at all times, remain in the Trust Department as such security. Provided, however, that should the Bank at any time desire to withdraw the Liberty Bonds herewith deposited, and substitute therefor other bonds of the United States of America, or Treasury Receipts of the Treasury Department of the United States of America of equal par value, it shall have the right so to do.

Upon the closing of said account, and only then, shall the said The First National Bank of El Paso have the right to withdraw the said securities from its Trust Department.

IN WITNESS WHEREOF, the said The First National Bank of El Paso has caused this instrument to be executed in duplicate by its president attested by its Cashier or Assistant Cashier, and its corporate seal hereunto affixed, at El Paso, Texas, this 29th day of January, 1931, one copy being delivered to the Texas & Pacific Railway Company and one copy deposited with the Bonds with the Trust Department.

THE FIRST NATIONAL BANK OF EL PASO,
(Signed) F. M. MURCHISON,
President.

ATTEST:
(Signed) J. E. BENTON, Cashier,
(Seal of The First National Bank of El Paso)

STATE OF TEXAS,)
COUNTY OF EL PASO.)

I, H. W. Moore, Trust Officer of The First National Bank of El Paso, hereby acknowledge receipt to the Trust Department of the said Bank of the Bonds above named and upon the conditions therein set forth.

(Signed) H. W. MOORE,
Trust Officer,
The First National Bank of El Paso.

Filed April 5, 1932. D. H. Hart, Clerk.

Answer of Defendant to Amended Bill of Complaint.

To the Said Honorable Court:

Comes now S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, hereinafter styled Defendant, and subject to his Motion to Dismiss the Amend-

ed Bill of Complaint, and answering only in the event that said Motion be overruled, says in reply to the First Count of the Amended Bill of Complaint:

I.

This Defendant admits the allegations contained in Paragraphs I, II and III.

II.

Defendant does not have sufficient information to, upon his own knowledge, affirm or deny the allegations of sub-section 1 of Paragraph IV and therefore denies said allegations.

III.

Defendant admits the allegations contained in sub-section 2 of Paragraph IV with the exception that this Defendant denies that the pledging of the Liberty Bonds referred to and the making of the pledge agreement referred to was done in good faith and in the regular course of business of The First National Bank, and this Defendant denies that the officers of said Bank were authorized to make any such agreement, and denies that the Bank was authorized to make any such agreement, and denies that Plaintiff was entitled to rely on any such pledge, or any such agreement, with reference to such Liberty bonds, and further denies that the depositors of said Bank were benefitted by any of said agreements, and denies that the deposits and assets of the Bank were increased by reason of any such deposit of Liberty Bonds or by said agreement, and denies that the pledging of said bonds was necessary for said Bank to properly carry on its business, and this Defendant says that said pledge agreement was and is wholly unauthorized and void and of no effect, and all of the parties concerned

with said pledge were charged with knowledge of the invalidity of said pledge agreement.

IV.

1. Defendant admits the allegations contained in sub-section 1 of paragraph V, with the exception that this Defendant denies that the Plaintiff had on deposit in said Bank on September 4, 1931, any specific sums of money, and says that the First National Bank was, on said date merely indebted to the Plaintiff in the amount of $54,646.94, and said Railway Company was, as to said indebtedness, merely a general creditor of said Bank.

2. Defendant admits the allegations contained in sub-section 2 of Paragraph V with the exception that this Defendant denies that he ever received any sums of money belonging to Plaintiff, and denies that he wrongfully holds possession of the Liberty Bonds referred to, and he denies that said bonds were subject to any lien in favor of Plaintiff, and denies that Plaintiff has any rights in said bonds.

3. Defendant admits the allegations of sub-section 3 of Paragraph V.

V.

1. Defendant admits the allegations of sub-section 1 of Paragraph VI with the exception that Defendant denies the allegation that this Estate will be unable to pay to unsecured depositors more than 30% of the amount of their deposits. This Defendant does not have sufficient information to, at this time, allege upon his own knowledge the amount of the total dividends which will be paid to unsecured depositors.

2. Defendant denies the allegations contained in sub-section 2 of Paragraph VI.

VI.

1. Defendant denies the allegations of sub-section 1 of Paragraph VII.

2. Defendant denies the allegations contained in sub-section 2 of Paragraph VII with the exception that this Defendant admits that he intends to treat the Liberty bonds and the proceeds arising from the sale thereof as general assets of his trust for the use and benefit of all of the creditors of The First National Bank.

3. Defendant denies the allegations of sub-section 3 of Paragraph VII.

4. Defendant admits the allegations of sub-section 4 of Paragraph 7.

VII.

Defendant denies the allegations of sub-sections 1 and 2 of Paragraph VIII.

VIII.

Defendant denies the allegations contained in Paragraph IX.

WHEREFORE, the Plaintiff is not entitled to have or receive any relief at the hands of this Court, and this Defendant prays that Plaintiff take nothing and that as to the original suit brought by the Plaintiff this Defendant go hence without day and recover of and from the Plaintiff all costs in this behalf incurred.

ABE H. GOLDSTEIN
JONES, GOLDSTEIN, HARDIE & GRAMBLNG
THORNTON HARDIE
Solicitors for Defendant.

Filed May 25, 1932 (El Paso Division) D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas. By Flora L. Linker, Deputy Clerk.

Motion of The Texas and Pacific Railway Company, Cross-Respondent, to Dismiss Cross-Bill of S. O. Pottorff, Receiver, Cross-Complainant.

To the Honorable Charles A. Boynton, Judge of the United States District Court for the Western District of Texas:

Comes now the Texas and Pacific Railway Company, named as Cross-Respondent in Cross-Bill of S. C. Pottorff, Receiver of The First National Bank of El Paso, Cross-Complainant, filed herein on April 5, 1932, and moves the court to dismiss said Cross-Bill, because the same does not state any matters in equity entitling Cross-Complainant to have the liberty bonds insolved in this suit declared general assets of The First National Bank of El Paso, subject to administration by Cross-Complainant for the benefit of the general creditors and depositors of said bank, nor does said Cross-Bill state any matter in equity which entitles Cross-Complainant to the relief prayed for, nor are the facts, as stated, sufficient to entitled Cross-Complainant to any relief against this Cross-Respondent.

WHEREFORE, it prays the judgment of the court whether it shall further answer said Cross-Bill, and that it be dismissed with its costs.

S. N. RUSSELL,
M. E. CLINTON,

Attorneys for The Texas and Pacific Railway Company, Cross-Respondent.

Filed May 18, 1932, D. H. Hart, Clerk, By Flora L. Linker, Deputy.

Court's Oral Finding.

REMARKS AND RULING OF THE COURT AT CONCLUSION OF ARGUMENT IN ABOVE CASE FOLLOWIG TRIAL THEREOF.

THE COURT: Gentlemen, the Court finds much in the reasoning of Judge Dickinson in the dissenting opinion in the B. & O. case that appeals to this Court, as well as the decision of the majority of the Court.

The Court has read a case that probably counsel on both sides have also read, decision of the Supreme Court of the United States in the case of First National Bank vs. Missouri, reported in 263 U. S., which case is referred to and relied upon by the Court in the majority opinion in the case of Baltimore & Ohio Railway Company vs. Smith, in suport of the announcement of the Court in that decision, in which the Court there said: "It is admitted that whenever the Comptroller was asked for an opinion as to the power of national banks to pledge collateral to secure private deposits, in every instance, he has disapproved of such pledges and held that, in his opinion, national banks do not have that power. Such uniform and long-continued interpretation and practice of an act by the department charged with administering it has great weight and is persuasive as to its correct construction." Which has been cited by the defendant, and relied upon by defendant's counsel in this case. The Court cites several cases, among them, in support of that proposition, First National Bank in St. Louis vs. State of Missouri, in 263 U. S. 640, opinion rendered by Associate Justice Sutherland. This is a suit which was brought by the Attorney General of the State of Missou-

ri, seeking to have it declared unlawful for the First National Bank in St. Louis to establish a branch bank, and the Court felt as an incident in determination of that matter it was necessary for the Court to pass upon that which was being sought by the State of Missouri, applied to a national bank, and laws of the United States, and the Court said in their opinion it does not. "The extent of the powers of national banks is to be measured by the terms of the federal statutes relating to such associations, and they can rightfully exercise only such as are expressly granted or such incidental powers as are necessary to carry on the business for which they are established," and a number of cases are there cited.

Then again the Court says: "But it is said that"—quoting again from that opinion—"the establishment of a branch bank is the exercise of an incidental power conferred by Sec. 5136, Rev. Stats., by which national banking associations are vested with 'all such incidental powers as shall be necessary to carry on the business of banking.'"

And the Court went on in that decision further and holds that the establishment of a branch in another building on the same block, or adjacent thereto, which the management of that bank thought would add to their business, was not an incident to the transaction of that business; and the Supreme Court holds in that decision that was not an incident to such business, it was not a necessary incident to the conducting of the banking business.

The Court refers in that opinion to the fact that under the charter the bank shall have one place and office, place for the transaction of their business, and this called for another. But the Court was much impressed by that language used there, that "The extent of the powers of national banks is to be measured by the terms of the

federal statutes relating to such associations, and they can rightfully exercise only such as are expressly granted or such incidental powers as are necessary to carry on the business for which they are established."

Now, the Circuit Court of Appeals, in the majority opinion in the B. & O. case, holds that it is not necessary to the carrying on of their banking business to pledge their assets to secure private deposits.

When it comes to a question of multiplying or subtracting, as counsel might have suggested a moment ago, decisions on questions as to whether or not national banking associations possessed powers as an incident to the transaction of the banking business to pledge its assets, bonds, to secure private deposits, there may have been decisions, and are decisions, cited, gathered together and cited in this opinion of Judge Parker for the Fourth Circuit, in the case of Schumacher vs. Eastern Bank & Trust Company, reported in 52 F. (2d) commencing at page 925, and shown on page 927 of that opinion. Now, the Court does not find it is a matter of addition and subtraction as to the decisions holding that national banking associations under the Federal Statutes of the United States are not authorized to pledge assets and bonds to secure a private deposit. There is a clear-cut, complete absolute decision in the B. & O. case,—Baltimore & Ohio Railway Company vs. Smith, reported in 56 F. (2) 799, by the majority opinion of the Court in that case, wherein it is held directly and clearly that national banking associations do not possess under the statute, and not vested with authority to pledge bonds and assets to secure private deposits. And it is there held in that opinion, with which counsel on both sides in this case are entirely familiar, that "Power is thus given to conduct a banking business and all incidental power necessary to carry it on." And cites a number of cases. "Implicit power must be

found, if at all, in the words, 'all such incidental powers as shall be necessary to carry on the business of banking.' " The Court says: "There is no evidence showing that it is necessary. On the other hand, inference is fairly reasonable that thousands of successful banks have never exercised such power. It cannot be concluded from the evidence that the exercise of such power is necessary in order to carry on the business of banking successfully."

The Court further says: "A national bank has only the power expressly given it and such incidental powers as are necessary to carry on the business of the powers expressly given. In none of these acts is any mention whatever made of the power to pledge assets to secure private deposits. If Congress had intended to give such power to national banks, it would have expressly indicated such intention. The fact that it did authorize national banks to pledge their property to secure public deposits, but was silent as to private deposits, clearly indicates that it did not intend to give that power in the case of private deposits."

And, further, "The reports of the Senate and House committees, on the amendment of 1930 to the Banking Act, show that Congress intended to deny that power to national banks in the case of private deposits."

Then the Court continues further and states: "The pledging of the assets of a national bank to secure a private deposit is not fairly incidental or necessary to carry on the business of banking. Such a contract is not only voidable but wholly void and of no legal effect."

In that case it is contended by the appellants therein, as in this case by the plaintiff, that if the bank did not have the power to pledge its assets to secure private deposits in question the Receiver cannot compel the return of the security without paying the deposit balance. The

Court goes on further there and holds a Receiver has power to renounce a contract, being void and illegal.

That is the opinion of a majority of the Court, of the Circuit Court of Appeals, in a case that the Court thinks exactly similar to the case now before the Court here. There is a dissenting opinion in that case. The authorities are reviewed at length by the majority opinion in that case.

Now, the Court does not find that the opinion of the Circuit Court of Appeals for the Fourth Circuit in the case of Schumacher vs. Eastern Bank & Trust Co., reported in 52 F. (2d) 925, or by that Court, the same Circuit Court of Appeals, in the case of Burrowes vs. Nimocks, 35 F. (2d) 152, 155, in any manner conflicting with the direct, clear, decisive and definite holding of the Circuit Court of Appeals in the Third Circuit in the Baltimore & Ohio case. The two cases decided by the Circuit Court of Appeals for the Fourth Circuit rest upon different facts, and decided upon a different ground. The decision in each of said cases rendered by the Circuit Court of Appeals for the Third Circuit rests upon the ground that the Court finds that the matters there involved, transactions entered into, related to loans made of funds to the bank; the bank was in need of loans, and made the loans in proper and regular way, and put up collateral; and the Court held that the bank should turn over the collateral. There is an expression used, certainly obiter dicta, by Judge Parker in the Schumacher vs. Eastern Bank & Trust Co. case, that: "Although some of the cases draw a distinction between a pledge of assets to secure a deposit of public funds and a pledge to secure a private deposit, there would seem to be, in the absence of statute, no valid basis for such distinction." Now, that expression by that learned Judge in that decision, of thought or line of reasoning that he might exercise, per-

haps was not called upon to exercise it in deciding this case, expressly says so when he said: "But, without deciding what would be the rule in the case of an ordinary private deposit, we are satisfied that deposits by a bank, such as those involved here, made as loans to and for the accommodation of the bank in which they are made, do not come within that category." And therefore, under the general rule of law, any expression made by a Court in its opinion not necessary to the decision reached by the Court in the particular case decided, would be held as obiter dicta, clearly obiter dicta in the Baltimore & Ohio case against Smith. Therefore, we have a decision, rendered by the majority of the Court, of a Circuit Court of Appeals of the United States for the Third Circuit, not this Circuit, which is the Fifth Circuit, which is clear and decisive of issues and matters similar to those involved in the case here at bar; and under well recognized rules of procedure and practice, that which should govern and control a trial Federal Judge if there is no decision of the Supreme Court on the particular points involved, or by the Circuit Court of Appeals for the Circuit in which the trial Court is situated, but there is an opinion by a Circuit Court of Appeals of another Circuit, that the trial Court of another Circuit should follow that decision of the Circuit Court of Appeals rendered in another Circuit. The Court here finds that controlling and binding on this Court, and the Court in this case will therefore render judgment and decree that the plaintiff take nothing by reason of their suit and action in this case; and the Court will decree, for whatever it is worth, if you want to avail yourselves of it, that you are entitled to recovery only as a general claim, and plaintiff is not entitled to recover the bonds put up on deposit, or any lien against said bonds, and the contract relating to the same is declared by the Court to be invalid and void;

that plaintiff would not be entitled to any recovery herein other than as a general creditor as against the Receiver. And the Court will render decree in favor of the Receiver on the cross action, for the quieting of title and rights of the Receiver in and to the particular bonds described and alleged to have been pledged in this matter.

The Court will overrule the motion,—probably should have done that in the first instance,—will overrule the motion to dismiss interposed by the defendant to the action of the plaintiff herein, as the Court now renders, is rendering decree, having heard the matter upon the merits and testimony, rendering decree in favor of the defendant. And also overrules the motion to strike of the Complainant on the cross action of the defendant.

As the Court has announced before, that under Rule 70½, in all equity cases, it is required that the Court make findings of fact and conclusions of law. The Court will ask counsel for the defendant to prepare findings of fact and conclusions of law and submit the same to the Court, and they may submit a copy to counsel on the other side; and also draft of decree, and if counsel for the Complainant desire to make any request of the Court for specific findings of fact or conclusions of law that may be done, and the Court will reconcile the same as the final findings.

The State of Texas,
County of El Paso.

I, Roy Lassetter, Shorthand Reporter, hereby certify that the foregoing is a true and correct copy of the remarks and ruling of the Court, at conclusion of argument and trial of the case of Texas and Pacific Railway Company vs. S. O. Pottorff, Receiver, First National

Bank of El Paso, No. 251 Equity, United States District Court in and for the Western District of Texas, El Paso Division thereof; said remarks and ruling being made by the Court on Thursday, May 26, 1932.

Witness my hand at El Paso, Texas, this 22nd day of August, A. D. 1932.

ROY LASSETTER
Shorthand Reporter.

Filed Aug. 22 1932. (El Paso Division) D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas, By J. N. Phillips, Deputy Clerk.

Finding of Facts.

(See page 88).

Conclusions of Law.

(See page 95).

Plaintiff's Objections and Exceptions to Conclusions of Law.

(See page 97).

Order Overruling Plaintiff's Objections and Exceptions to Conclusions of Law.

(See page 101).

Judgment.

BE IT REMEMBERED that on the 25th day of May, 1932, the above styled and numbered cause came on to be regularly heard; and thereupon, Defendant presented his Motion to Dismiss the Amended Bill of Complaint, and the Court announced that he would reserve his decision on said Motion until the conclusion of the case, to which all parties assented; and thereupon, the Plain-

tiff presented its Motion to Dismiss the Cross-Complaint of the Defendant, and the Court announced that he would reserve his decision on said Motion until the conclusion of the case, to which both parties assented; and thereupon, the pleadings were read, and the evidence introduced and the proceedings in the case continued until the 26th day of May, 1932, when all parties announced that they had completed the introduction of testimony; and thereupon, the Court, upon consideration of the pleadings and the evidence, and upon hearing argument from counsel for both parties, overruled the Motion of the Defendant, S. O. Pottorff, Receiver of the First National Bank of El Paso, Texas, to dismiss the Amended Bill of Complaint, and also overruled the Motion of the Plaintiff, The Texas and Pacific Railway Company, to dismiss the Cross Complaint theretofore filed by the Defendant, to which last action of the Court the Plaintiff duly excepted.

And now, on this the 26th day of May, 1932, the Court finds that the Plaintiff, The Texas and Pacific Railway Company, is not entitled to have or recover any relief herein against the Defendant, S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas. The Court further finds that the Defendant is entitled to have an Order and Judgment decreeing that the pledge contract dated the 29th day of January, 1931, and by the terms of which the said The First National Bank of El Paso, Texas, purported to create a lien in favor of the plaintiff upon seven United States Government Fourth Liberty loan four and one-quarter coupon bonds, 1933 to 1938, of the aggregate principal amount of $50,000.00, described by numbers and amounts as follows:

G00129907	$ 5,000.00
A00115901	5,000.00

E00040105	5,000.00
K00129870	5,000.00
G00353057	10,000.00
H00353058	10,000.00
H00298068	10,000.00

was and is void and of no effect, and entitled to have Judgment decreeing that said Liberty bonds are a part of the general assets of The First National Bank of El Paso, Texas, which passed to and became the property of the Defendant, and that same constitute assets to be administered by him for the benefit of the general creditors of the First National Bank.

IT IS THEREFORE, on this day, ORDERED, ADJUDGED and DECREED by the Court that the Plaintiff, The Texas and Pacific Railway Company take nothing by this suit, and that as to Plaintiff's suit the Defendant recover of and from Plaintiff all costs in this behalf incurred.

IT IS FURTHER ORDERED, ADJUDGED and DECREED by the Court that the pledge agreement above described was and is void and of no force and effect.

IT IS FURTHER ORDERED and DECREED that any cloud existing on the Defendant's title to said Liberty bonds by reason of the above mentioned contract, and by reason of the assertion of any claims to said bonds by the Plaintiff be, and the same is hereby removed.

IT IS FURTHER ORDERED and DECREED that said Liberty bonds are the property of the Defendant, constituting assets of his trust, to be administered by him for the benefit of the general creditors of The First National Bank of El Paso, Texas, and it is further OR-

DERED that the Plaintiff, The Texas and Pacific Railway Company, desist from asserting any further rights or claims in said Liberty bonds.

IT IS FURTHER ORDERED that the Defendant recover of and from the Plaintiff his costs in this behalf incurred, and that all writs necessary and proper for the collection of such costs issue, and that the officers of the Court have their writs against the respective parties for the costs by each of said parties respectively incurred, to all of which action of the Court the Plaintiff, in open court, duly excepted.

CHARLES A. BOYNTON,
Judge.

O. K.:
T. HARDIE
O. K. DEL W. HARRINGTON
S. N. RUSSELL

Filed June 21, 1932 (El Paso Division) D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas, By Flora L. Linker, Deputy Clerk.

Statement of Evidence and Bill of Exceptions.

BE IT REMEMBERED, That on this Wednesday, May 25, A. D. 1932, the above entitled and numbered cause came on for trial before the Honorable Charles A. Boynton, a United States District Judge in and for the Western District of Texas, at El Paso, Texas; the Complainant being represented by S. N. Russell, Esq. and D. W. Harrington, Esq., of El Paso, Texas, and M. E. Clinton, Esq., of Dallas, Texas, and the defendant being represented by Messrs. Jones, Goldstein, Hardie & Grambling, of El Paso, Texas; during the trial of which said cause the following facts were adduced in evidence,

objections made, and exceptions reserved by the parties:

The pleadings of the parties were read to the Court.

Motions to dismiss and motions to strike were presented to the Court, and ruling withheld by the Court until the following developing of the facts in the case.

The following stipulation and agreed statement of certain facts was introduced, and read to the Court:

(Omitting the style and number of the case).

The parties to the cause styled, numbered and pending as above, in part submit the matters in controversy between them to the courts upon the following agreed statement of facts:

I

(a) The Texas and Pacific Railway Company was on January 1, 1931, and at all times thereafter and now is a corporation duly chartered, organized and existing under and by virtue of the laws of the United States, to-wit: An Act of Congress entitled "An Act to incorporate the Texas Pacific Railroad Company, and to aid in the construction of its road, and for other purposes," approved March 3, 1871, and Acts amendatory thereof and supplementary thereto, including an Act of Congress approved May 2, 1872, whereby, among other things, the name, style and title of said Texas Pacific Railroad Company was changed to "The Texas and Pacific Railway Company." A copy of said Acts of Congress is attached hereto, marked Exhibit "A" and made a part hereof.

(b) The Texas and Pacific Railway Company has its principal office and place of business at Dallas in Dallas County in the Dallas Division of the Northern District of Texas, and owns and operates in interstate and

in intrastate commerce a line of railroad from New Orleans in the State of Louisiana to El Paso in the State of Texas, over which a large volume of interstate traffic is constantly moving; and as such carrier is subject to all applicable provisions of the Interstate Commerce Act, as amended in 1920.

II

S. O. Pottorff, Receiver of the First National Bank of El Paso, is the duly appointed, qualified and acting Receiver of said bank, an insolvent national banking association, and is now residing in and acting as such Receiver in El Paso County of the El Paso Division of the Western District of Texas.

III

This is a suit in equity which the District Court of the United States for the Western District of Texas, El Paso Division, is given original jurisdiction by Section 41, paragraphs 1 and 6, Title 28, and by Section 94, Title 12, of the Code of Laws of the United States, as revised and enacted by Congress on June 28, 1926, and approved on June 30, 1926.

IV

The Texas and Pacific Railway on July 3, 1922, was being operated by J. L. Lancaster and Charles L. Wallace, Receivers appointed by the District Court of the United States in and for the Western District of Louisiana, Monroe Division, and on said date upon petition filed by said Receivers, an order was made and entered by said Court authorizing said Receivers to select The First National Bank of El Paso as an additional depository for receivership funds, which order, among other things, provided that said bank "shall be required to furnish bonds

with good and solvent sureties * * * * in such an amount as will substantially equal the estimated average balances to be carried by said Receivers in said bank." A copy of said petition and order is attached hereto, marked Exhibit "B" and made a part hereof.

V

The First National Bank of El Paso, as principal, and National Surety Company, as surety, on July ....., 1922, executed and delivered to J. L. Lancaster and Charles L. Wallace, Receivers of The Texas and Pacific Railway Company, their certain surety bond for the sum of $25,000.00 conditioned as required by the aforesaid order of said Court, and thereupon said Receivers opened an account with said bank and made deposits therein approximately in the amount of said surety bond. A copy of said surety bond is attached hereto marked Exhibit "C" and made a part hereof.

VI

Said receivership of The Texas and Pacific Railway Company was terminated on or about May 14, 1924, and upon written request of The Texas and Pacific Railway Company, said The First National Bank of El Paso, as principal, and National Surety Company, as surety, on or about August 7, 1924, executed and delivered to said railway company a new surety bond in the sum of $25,000.00, payable to the Texas and Pacific Railway Company, a copy of which bond is attached hereto, marked Exhibit "D" and made a part hereof.

VII

The deposits of The Texas and Pacific Railway Company with The First National Bank of El Paso increased

during the month of April, 1927, and upon the written request of said railway company, The First National Bank of El Paso, as principal, and Maryland Casualty Company, as surety, on or about April 25, 1927, executed and delivered to The Texas and Pacific Railway Company an additional surety bond in the sum of $25,000.00, a copy of which bond is attached hereto, marked Exhibit "E" and made a part hereof.

VIII

(a) That on or about January 29, 1931, the officers of said The First National Bank of El Paso, while said bank was solvent and a going concern, with the full knowledge and approval of the board of directors of said bank, and pursuant to a certain substitution agreement between the officers of said bank and the officers of said railway company, deposited in the Trust Department of said bank with its Trust Officer, its certain (7) United States Government Fourth Liberty Loan 4¼ Coupon Bonds, 1933-38, of the aggregate amount and value of $50,000.00, described by numbers as follows, to-wit:

G00129907	$5,000.00
A00115901	$5,000.00
E00040105	$5,000.00
K00129870	$5,000.00
G00353057	$10,000.00
H00353058	$10,000.00
H0029068	$10,000.00

Said liberty bonds were so deposited with said Trust Officer separate and apart from all assets and securities of said bank, and in a separate envelope or receptacle bearing the name of said railway company, together with a copy of that certain trust agreement executed on or about January 29, 1931, by said First National Bank of

El Paso, acting by and through F. M. Murchison, its president, and J. E. Benton, its cashier, with the full knowledge and approval of the board of directors of said bank. A copy of said trust agreement is attached hereto, marked Exhibit "F" and made a part hereof.

(b) Thereupon, said surety bonds were cancelled as of January 30, 1931, and The Texas and Pacific Railway Company thereafter relied upon said liberty bonds and upon said agreement of said The First National Bank of El Paso as security for the repayment, upon its demand, of all monies deposited to its credit in said bank.

(c) But for said agreement of said officers of The First National Bank of El Paso and the aforesaid agreement of said bank and the deposit of said liberty bonds as aforesaid, The Texas and Pacific Railway Company would not have permitted the cancellation of said surety bonds; or, had they been cancelled said railway company would have immediately withdrawn all monies on deposit to its credit in said The First National Bank of El Paso and would have closed its account with said bank.

IX

(a) After said trust agreement had been executed and said liberty bonds had been deposited with said Trust Officer as aforesaid, and in reliance thereon, The Texas and Pacific Railway Company continued to make deposits in said The First National Bank of El Paso and maintained an average daily deposit in said bank in excess of $50,000.00; and said bank continued to accept and pay said railway company's checks and drafts drawn against its said deposits until on or about September 4, 1931, when said bank failed, became insolvent, closed its doors to the public and refused to accept, honor or pay any other or further checks or drafts drawn by said railway company against said deposits.

(b) The Texas and Pacific Railway Company had on deposit to its credit in said bank on September 4, 1931, the sum of $54,646.94, including accrued interest, which sum of money it was entitled to receive of and from said bank upon demand, and which sum of money, except the accrued interest, said railway company had collected for common services rendered in the transportation of both interstate and intrastate commerce.

(c) The Comptroller of the Currency of the United States, on or about September 6, 1931, duly and regularly appointed S. O. Pottorff, Receiver of said The First National Bank of El Paso, and said Receiver on or about September 8, 1931, took charge of all the affairs, assets and securities of said bank, and said Receiver on said date also took possession of the Trust Department of said bank in which said liberty bonds were held as security for the deposits of monies by said railway company in said bank, as aforesaid, and said Receiver has ever since said date held said bonds and now holds the same in his possession.

(d) The Texas and Pacific Railway Company, acting by and through its duly authorized officers and agents, seasonably made demand upon said Receiver for the payment to it of the same sum of $54,646.94, which sum said Receiver refused and now refuses to pay.

(e) The Texas and Pacific Railway Company, acting by and through its duly authorized officers and agents, seasonably demanded that said Receiver turn over to said railway company said liberty bonds, and that he credit its claim against said Receiver with the market value of said bonds at the time of said delivery, which demand said Receiver refused and now refuses.

(f) That upon the refusal of said Receiver to turn over to The Texas and Pacific Railway Company said

liberty bonds as aforesaid, it, acting by and through its duly authorized officers and agents, demanded that said Receiver sell said liberty bonds and apply the proceeds from the sale thereof to the liquidation of said railway company's claim, which said demand said Receiver refused and now refuses to comply with.

X

Said Receiver of the First National Bank of El Paso is unable to pay the unsecured depositors of said bank the full amount of their deposits.

XI

(a) The facts set out above are agreed to by the parties to this case, each reserving the right to object to any of the facts set out that they consider cannot legally be considered as evidence on the trial of this case, and each party reserves the full and complete right to introduce any further testimony, facts or documents that it, or they may desire, and to introduce *testiny* supplemental to or completing in any way the facts agreed to, each party at all times reserving the right to make any objection as to the admissibility of the same that it may see fit.

(b) This agreed statement of facts shall be filed with the papers in this cause, and the same shall constitute a part of the record herein.

Witness the hands of the attorneys of record for the respective parties.

(Signed) S. N. RUSSELL,
M. E. CLINTON,
Attorneys for Plaintiff, The Texas and Pacific Railway Company.

JONES, GOLDSTEIN, HARDIE & GRAMBLING,
(Signed) A. H. GOLDSTEIN,
By T. HARDIE,
Attorneys for Defendant, S. O. Pottorff, Receiver of the First National Bank of El Paso.

Attached to the Agreed Statement of Facts, and made a part thereof, is certified copy of Complainant's Charter and amendments, as referred to in Paragraph I, Subdivision (a), of the Agreed Statement of Facts.

Section 19 of the original Charter granted to the Texas Pacific Railroad Company provides as follows:

"Sec. 19. That the Texas Pacific Railroad Company shall be, and it is hereby declared to be, a military and post road; and for the purpose of insuring the carrying the mails, troops, munitions of war, supplies, and stores of the United States, no act of the company nor any law of any State or Territory shall impede, delay, or prevent the said company from performing its obligations to the United States in that regard: Provided, that said road shall be subject to the use of the United States for postal, military, and all other governmental services, at fair and reasonable rates of compensation, not to exceed the price paid by private parties for the same kind of service, and the Government shall at all times have the preference in the use of the same for the purposes aforesaid."

IN THE DISTRICT COURT OF THE UNITED STATES IN AND FOR THE WESTERN DISTRICT OF LOUISIANA.
MONROE DIVISION.

B. F. BUSH, Receiver of the railroads, etc., of St. Louis, Iron Mountain & Southern Railway Company,

Complainant, No. 1120

against In Equity

THE TEXAS AND PACIFIC RAILWAY COMPANY,

Defendant.

To the Honorable, Rufus E. Foster, Judge of said Court:

The petition of J. L. Lancaster and Charles L. Wallace, Receivers herein, would respectfully represent that by an order made herein on the 4th day of November, 1916, certain banks located at various points along the line of road in charge of your Receivers were designated as depositories of the funds of the Receivers.

Your petitioners would state that El Paso, Texas, is at the extreme Western Termini of the line of road in their charge, and that the State National Bank of El Paso was designated depository by the order of November 4, 1916.

Your petitioners would respectfully state that, in their opinion, an additional depository should be had at El Paso, and that it is to the interest of your Receivers to have the Court designate the First National Bank of El Paso as a bank in which your Receivers are authorized to deposit their funds.

The said First National Bank of El Paso, is the largest bank in El Paso, is solvent in every way, and is in a condition to be of service to your Receivers in many ways.

That said bank will comply with the order of Court applying to other depositories and will give bond to protect your Receivers against any loss.

J. L. LANCASTER AND
CHARLES L. WALLACE

Receivers of The Texas and Pacific Railway Company.

(Signed) By THOMAS J. FREEMAN,
General Counsel for Receivers.

EXHIBIT A.

ORDER

Upon the filing and reading of the foregoing petition, and upon consideration thereof, it is ordered that the Receivers herein are authorized to select as an additional depository of the funds of the Receivers, the First National Bank of El Paso, Texas.

That said First National Bank of El Paso, Texas, shall be required to furnish bond with good and solvent sureties, (either corporation or individual) in such an amount as will substantially equal the estimated average daily balances to be carried by said Receivers in said bank.

Thus done and signed, this the 3rd day of July, 1922.

(Signed) RUFUS E. FOSTER,
United States District Judge.

Filed July 6, 1922
W. Lee, Clerk,
U. S. Dist. Court,
Western Dist. of Louisiana.

EXHIBIT B.

DEPOSITORY BOND

The State of Texas,
County of El Paso.

KNOW ALL MEN BY THESE PRESENTS, That we, The First National Bank of El Paso, Texas, as principals, and .....

as sureties, acknowledge to owe and be indebted jointly and severally to John L. Lancaster and Charles L. Wallace, Receivers, of The Texas and Pacific Railway, and their successors in office, in the sum of TWENTY-FIVE THOUSAND DOLLARS ($25,000.00) for the payment of which well and truly to be made, we hereby bind ourselves, our successors, assigns and legal representatives jointly and severally.

In witness whereof we have hereunto set our hands at EL PASO, TEXAS, this ..... day of July, A. D. 1922.

But the above obligation is subject to the following condition: That if the said THE FIRST NATIONAL BANK OF EL PASO, TEXAS, shall well and truly on demand, pay over and deliver to the said John L. Lancaster and Charles L. Wallace, Receivers, as aforesaid of The Texas and Pacific Railway, or their lawful successors in office, all and such sums of money, funds and valuables, general and special, as may now be on deposit, and as may be deposited hereafter by said Receivers or their lawful successors in office, or that may come into custody or control of said THE FIRST NATIONAL BANK OF EL PASO, TEXAS, for account of said Receivers, then and in that case the above obligation shall become null and void; otherwise to remain in full force and effect.

THE FIRST NATIONAL BANK OF
EL PASO,

By .....
President.

.....

.....

.....

.....

ATTEST:

.....

Cashier

EXHIBIT C.

THE STATE OF TEXAS,
COUNTY OF EL PASO.

KNOW ALL MEN BY THESE PRESENTS, That We, The First National Bank of El Paso, Texas, as principals, and The National Surety Company of New York, as surety acknowledge to owe and be indebted jointly, severally and in solido to The Texas and Pacific Railway Company, in the sum of TWENTY-FIVE THOUSAND DOLLARS ($25,000.00) for the payment of which well and truly to be made, we hereby bind ourselves, our successors, assigns and legal representatives jointly, severally and in solido.

IN WITNESS WHEREOF we have hereunto set our hands at El Paso, Texas, this 7th day of August, A. D. 1924.

But the above obligation is subject to the following condition: That if the said The First National Bank of El Paso, Texas, shall well and truly, on demand, pay over and deliver to The Texas and Pacific Railway Company, or its order, all and such sums of money, funds and valuables, general and special, as may now be on deposit by, in favor of, or in the name of The Texas and Pacific Railway Company with the said The First National Bank of El Paso, Texas, and as may be deposited hereafter by The Texas and Pacific Railway Company or by any one for its account, with the said The First National Bank of El Paso, Texas, or that may come into the custody or control of said The First National Bank of El Paso, Texas, for account of The Texas and Pacific Railway Company, then and in that event the above obligation

shall become null and void; otherwise to remain in full force and effect.

In event it becomes necessary to enforce the obligation of this bond by suit, all costs of same, including attorney's fees, are to be paid by the principals and surety herein.

FIRST NATIONAL BANK,
EL PASO, TEXAS,
By JAMES G. McNARY,
President.

ATTEST:
(Signed) J. E. BENTON,
Cashier.
(SEAL)

NATIONAL SURETY COMPANY,
Surety,
By A. M. CLARK,
Vice-President, Surety.

ATTEST:
A. C. MILLIKAN,
Asst. Secretary.
(SEAL)

EXHIBIT D.

MARYLAND CASUALTY COMPANY
BALTIMORE

DEPOSITORY BOND.

STATE OF TEXAS,
COUNTY OF EL PASO.

KNOW ALL MEN BY THESE PRESENTS:

That we, The First National Bank of El Paso, Texas, as principals, and MARYLAND CASUALTY COMPANY of Baltimore, Maryland, as surety, acknowledge to owe and be indebted jointly, severally and in solido

to The Texas and Pacific Railway Company, in the sum of TWENTY FIVE THOUSAND DOLLARS ($25,000.-00) for the payment of which well and truly to be made, we hereby bind ourselves, our successors, assigns and legal representatives jointly, severally and in solido.

IN WITNESS WHEREOF we have hereunto set our hands at El Paso, Texas, this 25th day of April, A. D. 1927.

But the above obligation is subject to the following condition: That if the said The First National Bank of El Paso, Texas, shall well and truly, on demand, pay over and deliver to The Texas and Pacific Railway Company, or its order, all and such sums of money, funds and valuables, general and special, as may now be on deposit by, in favor of, or in the name of The Texas and Pacific Railway Company with the said The First National Bank of El Paso, Texas, and as may be deposited hereafter by The Texas and Pacific Railway Company or by any one for its account, with the said The First National Bank of El Paso, Texas, or that may come into the custody or control of said The First National Bank of El Paso, Texas, for account of The Texas and Pacific Railway Company, then and in that event the above obligation shall become null and void; otherwise to remain in full force and effect.

In event it becomes necessary to enforce the obligation of this bond by suit, all costs of same, including attorney's fees, are to be paid by the principals and surety herein.

The Surety shall have the right to terminate its suretyship under this obligation by serving notice, in writing, of its election so to do, upon said The Texas and Pacific Railway Company, or its lawful representatives, and thereupon the said Surety shall be discharged from any and all liability hereunder for any default of the Prin-

cipal occurring after the expiration of thirty (30) days after the service of such notice.

WITNESS OUR HANDS AND SEALS.

FIRST NATIONAL BANK OF EL PASO,
By F. M. MURCHISON,
Vice-President.

ATTEST:
J. E. BENTON,
Cashier.
(SEAL)

MARYLAND CASUALTY COMPANY,
Surety,
By HERMAN A. TAYLOR,
Attorney-in-Fact.

(SEAL)

EXHIBIT E.

STATE OF TEXAS,
COUNTY OF EL PASO.

THIS INSTRUMENT WITNESSETH:

The Texas & Pacific Railway Company, a corporation, carries an open checking account with the undersigned, The First National Bank of El Paso, in El Paso, Texas, and desires to continue so to do, and the Bank desires to continue to hold the said deposit.

For the purpose of securing the said Texas & Pacific Railway Company against any loss that might possibly occur by reason of its continuance and maintenance of the said deposit, The First National Bank of El Paso has on this date deposited in its Trust Department, and with its Trust Officer, which fact is evidenced by the signed statement to that effect of the said Trust Officer hereto attached, United States Government Liberty

Bonds of the par value of Fifty Thousand ($50,000.00) Dollars, to be held by the said Trust Department, through its Trust Officer, in trust for the use and benefit of the said Texas & Pacific Railway Company. This is for the purpose of protecting it against loss as aforesaid, and it is agreed that the said Bonds shall, at all times, remain in the Trust Department as such security. Provided, however, that should the Bank at any time desire to withdraw the Liberty Bonds herewith deposited, and substitute therefor other bonds of the United States of America of equal par value, it shall have the right so to do.

Upon the closing of the said account, and only then, shall the said The First National Bank of El Paso have the right to withdraw the said securities from its Trust Department.

IN WITNESS WHEREOF, the said The First National Bank of El Paso has caused this instrument to be executed in duplicate by its President, attested by its Cashier or Assistant Cashier, and its corporate seal hereunto affixed, at El Paso, Texas, this 29th day of January, 1931, one copy being delivered to the Texas & Pacific Railway Company and one copy deposited with the Bonds with the Trust Department.

THE FIRST NATIONAL BANK OF
EL PASO,
(Signed) F. M. MURCHISON,
President.

ATTEST:
(Signed) J. E. BENTON,
Cashier.
(Seal of The First National Bank of El Paso).

STATE OF TEXAS,
COUNTY OF EL PASO.

I, H. W. Moore, Trust Officer of the First National

Bank of El Paso, hereby acknowledge receipt to the Trust Department of the said Bank of the Bonds above named and upon the conditions therein set forth.

(Signed) H. W. MOORE,
Trust Officer,
The First National Bank of El Paso.

EXHIBIT F.

ADMISSION: It was admitted by the parties that the Liberty Bonds now held by the Receiver are the same bonds that were pledged by the Bank to the Railway Company.

A. L. EWING,

a witness for Complainant, being first duly sworn, testified as follows:

ON DIRECT EXAMINATION:

My name is A. L. Ewing. I am Assistant Treasurer of The Texas and Pacific Railway Company. I have been an official of that company thirty years, as Paymaster and Assistant Treasurer. I have been Assistant Treasurer since 1919. My duties as Assistant Treasurer are to protect the cash received and disbursed.

The Texas and Pacific Railway Company has a policy with reference to having its bank accounts secured.

Q What is that policy?

COUNSEL FOR DEFENDANT: Now, if the Court please, I object to that; it is not material what the policy of The Texas and Pacific is with reference to its deposits.

THE COURT: The Court can hardly see the materiality of the policy the railroad corporation may

have followed or had. The question is here at issue what was done with reference to these particular funds.

COUNSEL FOR COMPLAINANT: It is admitted with reference to how this particular transaction was handled.

THE COURT: The Court does not see, in view of that, what the materiality is of what had been the policy.

COUNSEL FOR COMPLAINANT: If the Court please, for the purpose of the bill may it be shown that the testimony would be to the effect that that was the policy of the Texas and Pacific, and had been pursued for many years prior to this time?

THE COURT: The Court will be reasonably liberal in matters tried before the Court, and let these matters be elaborated. It appears to the Court the objection is probably well taken. I will overrule the objection and unless you connect it up—The Court does not see the materiality of it, but the Court is going to pass upon this testimony.

COUNSEL FOR DEFENDANT: We except.

Q What did you say the policy of the railway company was with reference to requiring security?

A To accept a depository bond to protect the deposits in the banks.

Q State whether or not the railroad company required security for its deposits in all banks in which it made deposits?

A Yes, sir, with one exception, and that was a small bank, a small account down in Louisiana, in the Hibernia Bank of New Orleans.

(Defendant declined to cross examine the witness).

(Witness excused)

FRANK M. MURCHISON,

a witness for Complainant, being first duly sworn, testified as follows:

ON DIRECT EXAMINATION:

My name is Frank M. Murchison. I was connected with The First National Bank of El Paso from January, 1920, to the time it closed its doors on September 4th of last year. I was first connected with the bank as Vice-President, and was elected President of the bank in January, 1930; I do not recall the exact date.

During my term as President The First National Bank carried a part of the Texas and Pacific Railway Company's account or money in El Paso. I think the bank first procured this company's deposits in 1924. I was then Vice-President of the bank.

The railroad company required security for its deposit in The First National Bank. After the receivership ended in about 1924 the bank was then required by the railway company to make bond to The Texas and Pacific Railway Company. It is my recollection that bond for the amount of $25,000.00 in the National Surety Company was first made by the bank to the railroad company for the purpose of securing its account. There was a premium charged by the insurance company on that bond, and the bank paid the premium.

Up to about January 29, 1931, the bank carried insurance security by which the T. & P. Railway Company's account in the Bank was secured by surety bonds in the amount of $50,000.00, and the bank paid the premiums on those bonds.

Some time in January, 1931, it was decided by me, as President of the bank, and some of the other officers of the bank, to save the premiums on the surety bonds by substituting Liberty Bonds as surety for the Texas and Pacific Railway Company's account, in lieu of those bonds. Mr. Benton and myself, as I recall it, were discussing this matter of the premiums on this bond, as well as another one or two, and that the bank had been paying; so we decided to take it up with The Texas and Pacific Railroad people, the matter of the substitution of bonds, of Liberty bonds for the surety bonds, in order to save this premium that the bank had been paying. With that in mind Mr. Benton, at my suggestion, went down to Dallas to see Judge Lancaster, and made an arrangement with him in connection with it.

Pursuant to Mr. Benton's visit to Dallas Liberty Bonds were pledged with the Trust Department of The First National Bank, and a trust agreement entered into. Mr. Benton handled the details with reference to handling of the bonds and of preparing the pledge agreement. He did that under my direction, I knew what was being done, and with my approval.

This is my signature (indicating), and this is Mr. Benton's signature. The third signature there is Mr. H. W. Moore's, Assistant Trust Officer and Assistant Cashier of The First National Bank.

The document, being marked "C-1", was introduced in evidence by Complainant; said document being the trust agreement, and being the same document as hereinbefore copied in full herein, marked "Exhibit F" to agreed statement of facts, and reference is here made to same.

My recollection is that the approximate average

amount of money that The Texas and Pacific carried in The First National Bank from the time of the termination of the receivership, from the time the second bond was required, up to the time that the Liberty Bonds were pledged in lieu of the surety bond, was approximately the amount of the bond, $50,000.00. After the substitution of the Liberty Bonds up to the time the bank closed on September 4, 1931, I think the average amount of money carried by the railway company in the bank was approximately $50,000.00.

Those deposits were made by the City Ticket Office and the El Paso Union Depot Company here in El Paso. I do not recall whether there were any outside deposits made here. The deposits I have mentioned were made daily. I am not in position to state the average amount of those daily deposits, not even approximately. Likewise I would not know the amount of withdrawals.

(Defendant declined to cross examine the witness).

(Witness excused).

J. E. BENTON,

a witness for Complainant, being first duly sworn, testified as follows:

ON DIRECT EXAMINATION:

My name is J. E. Benton. I was formerly Vice President and Cashier of The First National Bank here in El Paso. I was connected with that bank since February, 1903. I was made Vice-President of the bank I think in 1920, and held that position until it closed. I was also Cashier of the bank. I can't give you definite dates I was Cashier because I have been Cashier two or three times. When I was made Vice President another man was elected Cashier, and when he left the bank I was elected

Cashier, and then another party was elected Cashier, and when he left I was elected Cashier again.

I was Cashier in 1931.

The account of The Texas and Pacific Railway Company in The First National Bank was secured by a surety bond up to about the 29th of January, 1931. The First National Bank paid the premium on the bond.

At the instance of Mr. Murchison and other officers of the bank it was agreed to save the premiums on the surety bonds by substituting Liberty Bonds in lieu thereof, if such substitution would be agreeable to the officials of the railway company. In pursuance of that agreement by the officers of the bank I went down to Dallas and met Mr. Lancaster. He was taking the train for Cleveland and I rode from Dallas to Longview with him in the drawing room and explained the purpose of my visit, and that we wanted to substitute Liberty Bonds and cancel the depository bond.

That was Mr. J. L. Lancaster, President of The Texas and Pacific.

Q State what conversation you had with Mr. Lancaster with reference to the substitution of those bonds?

COUNSEL FOR DEFENDANT: I don't know the nature of the conversation, but I think it is wholly immaterial whatever the conversation might have been. Certainly we can't change the law by the bank trying to get Liberty Bonds substituted for a surety company bond with the railway company; I don't see how it could affect any issue in this case.

THE COURT: The Court is rather disposed to concur in the statement of the law as made by counsel for the defendant, but is disposed to allow a good deal of latitude in this testimony. They have an allegation here, I believe, that but for this being done

the deposit might be withdrawn, and so forth. The Court will overrule the objection.

Defendant excepted.

A I told him the purpose of my visit was to ask him to accept Liberty Bonds as surety on The Texas and Pacific account in The First National Bank in lieu of the depository bond. I told him it would save us $250.00 a year premium, and he in substance said he would permit that substitution provided that I could assure him that it was legal, and I told him that I would take it up with our attorneys when I got back and if it was not I would not ask him to go through with it; if it was I would have the papers drawn up by the attorneys for the bank, and send them to him.

Turney, Burges, Culwell & Pollard were attorneys for the bank.

With reference to whether Mr. Lancaster said anything with reference to the withdrawal of the account unless it was secured, Mr. Lancaster said that that time, "Of course, you know this is not my personal policy, it is the policy of the railway company to have their funds secured, that is deposited in banks, and what we want is security, and after your investigation if you tell me the way you propose to secure it is all right you can go on and do it."

I then returned to El Paso. I went up and told Mr. Burges of my interview with Mr. Lancaster, and the purpose of it, and asked him if that could be done.

Q What was his reply?

COUNSEL FOR DEFENDANT: I certainly do not think it is material to go into Mr. Burges' opin-

ion about the law; he certainly could not change the law by his opinion.

THE COURT: No, that is very true. The Court realizes your allegations, and will overrule the objection, and permit the testimony to be introduced.

A As I have stated, I told him of my conversation with Mr. Lancaster, and the purpose of my visit, and I wanted a contract drawn up, binding, so that we could put up Liberty Bonds as surety for the account; explained in detail the circumstances as I have said. He said that could be done, and drew the contract up.

Mr. Burges advised me that would be legal, the substitution of the Liberty Bonds for the surety bond. I then sent a copy, of one of the contracts, to Mr. Lancaster, and turned one of them over to Mr. Moore, Trust Officer of the bank, and attached the bonds to be placed in the trust agreement, with Mr. Moore as Trust Officer, in accordance with the terms of the contract. I presume those are the same Liberty Bonds described in the petition here.

That transaction was made in the regular course of the bank's business, in good faith.

Q Do you know whether the bank was benefitted or injured by the substitution of the Liberty Bonds for the surety bond?

COUNSEL FOR DEFENDANT: I think that calls pretty much for a conclusion.

THE COURT: The Court sustains the objection to this question. That is a matter that might be deduced from the testimony in the case; it might be a matter of conjecture, considerable speculation. The Court sustains the objection.

COUNSEL FOR COMPLAINANT: We except to the ruling of the Court.

Mr. Lancaster said, "This is not a personal policy of mine; it is the policy of the railroad company to insist upon security for funds placed in banks, so if you assure me it is good security you may go through with it."

I do not know the approximate amount of the daily deposits made in the bank by the railway company from the 1st of January, 1931, up to the time the bank closed. The average amount on deposit was around $50,000.00 all the time. There were withdrawals from the bank in various forms. There would be checks presented, drawn by Mr. Ewing's office, but I don't know to whom. I don't think they were to empolyees here in El Paso. More or less claim accounts or something of that sort; and then they transferred funds in larger amounts to depositories elsewhere.

Employees in El Paso cashed their pay checks with that bank. On the back of the pay check it provides "This check is payable at The First National Bank, El Paso," naming other banks on their line.

Q Was the bank benefitted in any other way other than by saving the premiums on the surety bond?

A Yes, sir.

Q In what other way?

A In the prestige it gained.

COUNSEL FOR DEFENDANT: We had an objection which was sustained.

THE COURT: The Court sustains the objection.

COUNSEL FOR COMPLAINANT: We except.

I was employed by The First National Bank approximately twenty-eight or thirty years. That bank was examined by the National Bank Examiners; I imagine two or three times a year, as much as twice a year, and maybe oftener. There was an examination made in August prior

to the time the bank closed in September. It seems to me like it was the beginning of August, probably the first week in August. There were probably six or seven or eight examiners who made the examination at that time.

These Liberty Bonds were placed in the Trust Department of the bank, and there was a record of that fact made in our books in the bank.

In that examination of the bank some examiners handled certain portions of the business and others other portions. The trust accounts ordinarily would have been inspected probably within a week after the inspection was commenced.

I don't know all of the powers of a bank examiner. It is my understanding they have authority to close a bank.

Q State if an irregularity or an unlawful transaction had been shown on the records of the bank's books, and that had been seen by a bank examiner what would they have done?

COUNSEL FOR DEFENDANT: He can't be going by his past experience in The First National Bank when he answers that question, certainly, what the bank examiners did in closing a bank as soon as he found irregularities in a National bank.

COUNSEL FOR COMPLAINANT: No, I am not saying that.

THE COURT: The Court sustains the objection. Now, as to what the bank examiner did do, if the bank examiner in making his report made some notation in reference to this deposit, as shown by the records of the bank, that probably would be the best evidence of what the bank examiner did. The answer elicited by this interrogatory calls for a conclusion of this witness of law and fact, in the opinion

of the Court. The Court sustains the objection.

COUNSEL FOR COMPLAINANT: We except, for the reason we expect to prove by the witness that if the Comptroller, who was then acting through his examiner, had contended that the placing of these Liberty Bonds in lieu of the other bonds was unlawful or beyond the powers of the bank, that the bank examiner would have immediately called the bank's attention to that fact, and required it to be remedied.

THE COURT: Very well. The Court sustains the objection.

Q Was there any complaint, Mr. Benton, to the officials of the bank by the examiner on account of the Texas and Pacific Railway Company's account being secured by these Liberty Bonds?

A Not that I know of, no, sir; I didn't hear of any.

Q Would you have known it if it had been made?

A Yes, sir.

COUNSEL FOR DEFENDANT: That calls for a conclusion of the witness.

Q Who would it have been made to?

THE COURT: The Court sustains the objection to the last question.

Q You say there was no complaint?

A There was no complaint made to me, no, sir, or anyone else that I know of.

Mr. Murchison was the executive in charge of the bank. Complaints of that nature would have been made to Mr. Murchison or to me, usually to Mr. Murchison; he was the head of the bank. I say usually. Most often, most always the case.

There was a saving to the bank by reason of its being

enabled to avoid payment of the premiums on the surety bond by reason of the substitution of the Liberty Bonds. The Liberty Bonds drew interest, and the bank received that interest.

ON CROSS EXAMINATION:

Q Mr. Benton, this report of the August examination of the bank was never finally completed and sent in to the Comptroller until after the bank closed, was it?

A Not to my knowledge, no, sir.

I said that the acceptance of the pledge of the Liberty Bonds by Texas and Pacific Railway Company was a benefit to the bank. As a matter of fact from the time that pledge of Liberty Bonds was made, from February, I believe, the deposits in the bank continuously decreased, up until the bank closed, the total deposits in the bank.

Q As a matter of fact when you told of the bank's reason for changing from a surety bond to the pledge of Liberty Bonds, you had already received a request from the Maryland Casualty Company in the form of a letter to relieve them from that guaranty, hadn't you?

COUNSEL FOR COMPLAINANT: We object to that as being wholly irrelevant, immaterial, and incompetent for any purpose in this case.

THE COURT: The Court will permit the witness to answer that question in view of the fact on direct examination this witness has been interrogated as to why the change was made, and as an incident that might be taken into consideration for determination as to the various reasons that may have prompted the change. The Court feels that perhaps it is proper, and probably is on cross examination, to ask the witness whether he had received notification

from the surety company to decline to further act. The Court will overrule the objection to that question, and allow that question to be asked.

COUNSEL FOR COMPLAINANT: We except.

THE COURT: The letter would be the best evidence. Is there objection on that ground?

COUNSEL FOR COMPLAINANT: Yes, sir, we make that objection.

COUNSEL FOR DEFENDANT: I want to show the witness had knowledge of that fact. This is not a case where we are suing on the letter, or suing on an instrument.

THE COURT: The Court overrules the objection.

COUNSEL FOR COMPLAINANT: We except.

A I don't know of any specific letter on that account from the Maryland Casualty Company.

Q You knew they had requested withdrawal from their depository bonds with The First National, didn't you?

A I didn't know that they made a general letter; I knew there was a ruling on it with Hudspeth County, and I knew Mr. Scales told us they were going to get off all bonds.

Q As a matter of fact, your real purpose, Mr. Benton, was to get the substitution made because you knew you were going to have to give up this Maryland Casualty bond?

A I don't think there is any doubt but what we would have eventually, but I don't think that they were notified.

Q That was the reason, purpose for the substitution, not for the saving of the $250.00 you had been paying eight or nine years?

A That was not all of it; that was not the only consideration, because we knew eventually they would ask to have the bond cancelled, or would not renew it. Mr. Scales had told us he had been instructed not to renew any more depository bonds.

Mr. Scales was the agent for the Maryland Casualty Company; he represented them here.

At the time I went to Dallas at the expense of the bank to get this substitution made I don't think we had been instructed or that Scales had told us about the depository bond; I don't think there was any specific instructions, but I absolutely knew what the attitude was. I did not know when they withdrew we could not get any other surety company, any standard insurance company, to take that risk, but I had a good hunch.

Q Especially in view of the record withdrawals of deposits from the bank?

A Scales had told us it was the policy of his company not to renew any more bonds.

ON REDIRECT EXAMINATION:

I did not mention to Mr. Lancaster at the time this substitution agreement was made, or at any other time thereafter; this substitution was desired on account of the surety company threatening to cancel its bonds. He never heard of that, as far as know. The bond provides that he was to be notified in case of cancellation, but I did not mention that in my discussion with Mr. Lancaster in any manner.

Mr. Scales did not tell me it was the attitude or disposition of his company to refuse to renew any surety bonds, but I got information in the bank that he had received a wire or letter to the effect not to write any more depository bonds.

Q For anybody? Was that general, or just for The First National?

A That is what he told us.

Q Mr. Benton, were any other accounts in the First National Bank secured by the bank?

COUNSEL FOR DEFENDANT: I fail to see the materiality of that question. I object to it on the ground it is immaterial to any issue in the case.

THE COURT: The Court does not see the materiality of that testimony, and the Court sustains the objection; or will hear from counsel as to why you consider the same as material, and without going too far adrift, necessitating the inquiring into conditions arising in connection with giving security in each and every instance the bank may have put up security.

COUNSEL FOR COMPLAINANT: It shows, your Honor, I think, the practice and custom, or probability of the knowledge on the part of the Comptroller, the bank was securing the general deposits, and general way of handling the banking business. Probably would tend to show that it is exercise of the power incident to carrying on the business to secure deposits, but I think it would be material, competent evidence.

THE COURT: You can ask him in general terms as to whether the bank put up security in connection with other deposits. I will permit that question to be asked. I even question the materiality of that. I will permit that question to be asked. It would not change the legal effect of it, in the opinion of the Court.

Q Was it the custom of the bank to secure deposits?

A Yes. sir.

The railway company's account was beneficial to the bank.

ON RECROSS EXAMINATION:

The bank furnished surety company bonds to secure deposits. We guaranteed deposits by surety bonds. I would imagine the bank had between 6,000 and 7,000 depositors. Out of those 6,000 or 7,000 deposits there were maybe six or eight or ten deposits secured by a surety bond at any one time, excluding the Government and such accounts as that. It was the custom of the bank to give security to a few of the corporations, six or eight or ten. I think that a great many of the corporations insisted on it, and some paid the premiums themselves, and others we paid the premiums on, but those that paid the premiums would exceed that six or eight or ten I mentioned. Those instruments were in the form of surety bonds. It was not a pledge of the assets of the bank. As far as I can remember this is the only case where a private account was secured by pledging the asset.

(Witness excused).

Complainant introduced in evidence the deposition of

JOHN L. LANCASTER,

taken before Houston Wood, a Notary Public in and for Dallas County, Texas, on May 13th, 1932, said witness testifying in answer to direct interrogatories as follows:

My name is John L. Lancaster; residence, Dallas, Texas. I am President of The Texas and Pacific Railway Company.

I was President of The Texas and Pacific Railway Company from May, 1917, to July, 1918, and have been

President of that company continuously from December, 1919, to the present date.

I came to The Texas and Pacific Railway in March, 1915, as Assistant to the First Vice-President, and served in that capacity until March, 1916. In that month I succeeded to the First Vice-Presidency and remained in that position until May, 1917, when I became President. I was appointed one of the receivers of The Texas and Pacific Railway by the United States District Court for the Western District of Louisiana, Monroe Division, in October, 1916, and acted as such receiver until July, 1918, and from December, 1919, to May 14, 1924, and during this last period Mr. Charles L. Wallace acted as my co-receiver of the property. In addition to this service for the period July, 1918, to December, 1919, I was Federal Manager of a group of railroads in the Southwestern Region including The Texas and Pacific Railway. For the past sixteen years I have been in responsible charge of the management and operation of The Texas and Pacific Railway Company and its subsidiary lines.

I, together with my co-receiver, petitioned the United States District Court for the Western District of Louisiana, Monroe Division, for an order authorizing us to select The First National Bank of El Paso as a depository for receivership funds. Mr. Wallace and I, by our counsel, Mr. Thomas J. Freeman, on or about the 3rd day of July, 1922, filed a petition in the United States District Court for the Western District of Louisiana, Monroe Division, requesting the Court to designate The First National Bank of El Paso as an additional depository of the funds handled by us as receivers of The Texas and Pacific Railway, and the Court on that date entered an order authorizing us, as such receivers, to select The First National Bank of El Paso as an additional depository of such receivership funds, directing

that said bank should furnish us with a bond, with good and solvent sureties—either corporate or individual—in an amount substantially equal to the estimated average daily balances to be carried by us as such receivers in that bank. I am attaching hereto a true and correct copy of the petition and order referred to, marked "Exhibit 1".

(The document in question is the document attached to the agreed statement of facts, marked Exhibit B, and reference is here made to same in the agreed statement of fact).

I advised the President of The First National Bank of El Paso that when the bank furnished us with an acceptable corporate surety bond as provided in the order of the Court, and in the amount of $25,000.00, we would open an account with that bank and would maintain an average daily deposit therein substantially in the amount of said bond. On or about July 10, 1922, The First National Bank of El Paso, as principal, and National Surety Company, as surety, executed and delivered to Mr. Wallace and me, as receivers of The Texas and Pacific Railway Company, a surety bond in the sum of $25,000.00, conditioned as required by said Court order and payable to us as such receivers. This surety bond was acceptable to us, and upon its receipt we opened an account with The First National Bank of El Paso and made deposits therein approximately in the amount of said surety bond.

The original corporate surety bond to which I referred was returned to the surety company at the close of the receivership of The Texas and Pacific Railway and I do not have a complete copy of that bond. However, I am attaching hereto a true and correct copy of the form of said surety company bond which was executed on or

about July 10, 1922, by The First National Bank of El Paso, as principal, and the National Surety Company, as surety in the amount of $25,000.00, payable to J. L. Lancaster and Charles L. Wallace as receivers of the Texas and Pacific Railway, as above stated.

(This document is the same as the one included in the agreed statement of facts, marked "Exhibit C", and reference is made to same in the agreed statement of facts).

The receivership of The Texas and Pacific Railway in the United States District Court for the Western District of Louisiana, Monroe Division, was terminated on May 14, 1924.

Since the termination of said receivership, I have held the position of President of The Texas and Pacific Railway Company.

When said receivership was terminated on May 14, 1924, the receivers had on deposit with The First National Bank of El Paso approximately $25,000.00 which was secured by the surety bond which I have described. Upon the termination of the receivership this account in the name of the receivers was placed in the name of The Texas and Pacific Railway Company and The First National Bank of El Paso was notified immediately to furnish The Texas and Pacific Railway Company with a new corporate surety bond in the sum of $25,000.00 to secure its said deposits.

On or about August 7, 1924, The First National Bank of El Paso, as principal, and National Surety Company, as surety, executed and delivered to The Texas and Pacific Railway Company a surety bond in the sum of $25,000.00 to secure its said deposits, and the old surety bond payable to the receivers was then cancelled.

The Texas and Pacific Railway Company continued its account with and thereafter made deposits in The First

National Bank of El Paso, its average daily deposit balance substantially equalling the amount of the new surety bond until about the month of April, 1927, when the average daily deposit balance in that bank increased to a sum considerably in excess of $25,000.00. Because of that increase, The First National Bank of El Paso was notified to furnish The Texas and Pacific Railway Company with a new corporate surety bond in the sum of $50,000.00, in lieu of the then outstanding surety bond in the sum of $25,000.00, to secure its said deposits. Instead of furnishing a bond in the sum of $50,000.00, The First National Bank of El Paso, as principal, and Maryland Casualty Company, as surety, on or about April 25, 1927, executed and delivered to The Texas and Pacific Railway Company an additional surety bond in the sum of $25,000.00, thereby increasing the total amount of such security to $50,000.00.

Both of these surety bonds, payable to The Texas and Pacific Railway Company, remained in full force and effect from the respective dates of their execution until and after January 29, 1931, and during that period The Texas and Pacific Railway Company kept an account with and made deposits in The First National Bank of El Paso, its average daily deposit balance substantially equalling the aggregate amount of said bonds.

I am attaching hereto a true and correct copy of each of the surety bonds, payable to The Texas and Pacific Railway Company, to which I have referred.

(The two documents are the same as shown in the agreed statement of facts, marked "Exhibit D" and "Exhibit E," and reference is here made to same in the agreed statement of facts).

During the month of January, 1931, Mr. J. E. Benton, Vice-President of The First National Bank of El Paso,

came to see me in Dallas about The Texas and Pacific Railway Company's account and deposits in that bank and the security for the same.

Mr. Benton stated to me that the officers of The First National Bank of El Paso, including its President, Mr. F. M. Murchison, desired The Texas and Pacific Railway Company to accept as security for its deposits at that time, and as security for its future deposits, United States Government Liberty Loan Bonds of the par value of $50,000.00, in lieu of the then outstanding corporate surety bonds payable to The Texas Pacific Railway Company which were then fully protecting and securing its deposits in that bank. In explanation of this request, Mr. Benton stated that the bank had been required by the railway company to furnish it with corporate surety bonds to secure its deposits, the premiums on which were very expensive and a burden on the bank, and they asked that I agree to the substitution of the liberty bonds in lieu of the surety bonds in order to relieve the bank of those heavy premium payments. I told Mr. Benton that it was the policy of The Texas and Pacific Railway Company to require ample and adequate security for its deposits, preferably corporate surety bonds, that under no circumstances would I continue The Texas and Pacific Railway Company's account with and deposits in The First National Bank of El Paso without full and adequate security, and if the then outstanding corporate surety bonds were cancelled without the substitution of other security acceptable to the railway company, its account with said bank would be closed and its deposits withdrawn, but if the substitution of liberty bonds which he proposed would afford The Texas and Pacific Railway Company the same security as the then outstanding corporate surety bonds, I would agree to such substitution solely for the purpose of enabling the bank to save the

premiums on said corporate surety bonds. Mr. Benton stated to me that the liberty bonds would protect The Texas and Pacific Railway Company's deposits as fully as they were protected at that time by the corporate surety bonds, and, believing and relying upon his representations, I told him to have the officers of the bank and the bank's attorneys prepare an agreement which would secure The Texas and Pacific Railway Company's deposits as fully as the then outstanding corporate surety bonds and upon receipt of such instrument we would agree to the cancellation of those surety bonds. Mr. Benton took his departure stating that he would attend to the matter accordingly and at once.

On the 31st day of January, 1931, I received from Mr. Benton an instrument in writing which he stated had been prepared by the attorneys for The First National Bank of El Paso, and which was executed by that bank on the 29th day of January, 1931, by F. M. Murchison, its President, and J. E. Benton, its Cashier, which instrument recited:

"For the purpose of securing the said Texas & Pacific Railway Company against any loss that might possibly occur by reason of its continuance and maintenance of the said deposit, The First National Bank of El Paso has on this date deposited in its Trust Department, and with its Trust officer, which fact is evidenced by the signed statement to that effect of the said Trust Officer hereto attached, United States Government Liberty Bonds of the par value of Fifty Thousand ($50,000.00) Dollars, to be held by the said Trust Department, through its Trust Officer, in trust for the use and benefit of the said Texas & Pacific Railway Company. This is for the purpose of protecting it against loss as aforesaid, and it is agreed that the said Bonds shall, at all times, remain in the Trust Department as such security."

Upon the further representation of Mr. Benton that the bank's attorneys had carefully considered the substitution agreement, had pronounced it legal and valid in every particular and that it was a binding and enforceable obligation against The First National Bank of El Paso, and protected the Texas and Pacific's deposits in said bank as fully as said outstanding surety bonds, and believing those representations to be true, I accepted said liberty bonds, which had been placed in the hands of Mr. H. W. Moore, Trust Officer of said bank, in accordance with the terms of the agreement, in lieu of the then outstanding corporate surety bonds which were then protecting the deposits of The Texas and Pacific Railway Company in that bank, and relying upon said liberty bonds as security for said deposits I caused said surety bonds to be cancelled as of January 30, 1931. After such substitution had been effected, The Texas Pacific Railway Company continued its account with and its deposits in The First National Bank of El Paso, its average daily deposit balance substantially equalling the total par value of said liberty bonds.

I am attaching hereto as my answer to this interrogatory a true and correct copy of said written instrument executed by The First National Bank of El Paso.

(The document is the same document marked "Exhibit F" attached to and forming part of the agreed statement of facts, and reference is here made to same in the agreed statement of facts herein).

On September 4, 1931, The First National Bank of El Paso owed The Texas Pacific Railway Company the sum of Fifty-four thousand, Six Hundred Forty-six and 94/100 Dollars. Possibly there is a small amount of interest included but I do not know the amount.

S. O. POTTORFF,

a witness for Complainant, being first duly sworn, testified as follows:

ON DIRECT EXAMINATION:

I am the Receiver of The First National Bank here in El Paso.

There were no examinations made by the bank examiners of the condition of the bank from the 29th day of January, 1931, until August 6, 1931. There was one examination made between the 29th of January, 1931, and September 6th, 1931. That examination began at 8:00 o'clock in the morning, August 6th, and ended at noon on August 20th. The examiner was Jacob Embry. I don't know the names of his assistants. I think Mr. Collier was here, in charge, although I was not here. His name does not appear on the report. I do not know the number of examiners that were present, and the report does not show it. There was one examiner, and he had some assistants.

With reference to what the report shows with reference to The Texas and Pacific Railway Company's account in the bank being secured, the line across the report under the caption of Bonds and Securities, which lists all the bonds and securities owned by the bank, both pledged and unpledged, there is one line extending across the page showing where there were $50,000.00 of Liberty Bonds — that line says $50,000.00, 4-4¼ Liberty Loan Bonds, 33-38, $50,000.00, estimated market value $52,339.55. The first $50,000.00 that I mentioned is under the caption, under the column headed, entire number of shares of stock or value of bonds and state whether or not stocks or bonds. The second column is headed, name and issuing corporation, character of mortgage, rate, maturity. Under the second column is 4-4¼ Liberty Loan

Bonds. That is abbreviated, L. L. B., 33-38. That means date of maturity, 1933 to 1938; optionally in 1933, mature in 1938. Third column, amount at which carried on books, $50,000.00. Fourth column, estimated market value, $52-339.55. Of course Liberty Bonds have daily quotations, fluctuate. Last column, indicate whether taken for D. P. C., abbreviation for debt previously contracted, and where interest or dividend is not paid, and indicate those loaned or pledged, and if any borrowed so state, are not any valuable security charged off. See note below. In that column appears, secure T. & P. Railway deposit.

This report shows that The Texas and Pacific deposit on that date was secured by Liberty Bonds of the par value of $50,000.00, and also shows the market value at a greater amount.

I never was a bank examiner. When I take charge of a bank it is past its days of being examined. When I take a bank all of its examinations have been made. I just see the results of the examination, filed copies of the reports. I am never in attendance at an examination because I get there after it is done. I am more or less familiar with what an examiner does from the reports. I could not tell the day the examiners made examination of the securities of this railway; very likely was the first day the examination started, because the first thing the examiners do when they come is verify the cash and check up the securities. After they balance and check over the cash and securities they generally go into the loans owned by the bank, whether pledged or unpledged. Bearing in mind I have never examined a bank, ordinarily one of the first things is to balance the cash, as I understand it; the next thing is to see all securities are in their proper place.

Q And if they are not in the proper place they report that to the Comptroller?

A The report goes on the regular form here, just as it is there, reflecting the bank's books, what the bank's books show. An examiner may make a special report by letter on something that requires that sort of a report.

Q If the bank had made some irregular transaction, and that fact is shown by its books, and the examiner had discovered such transaction, would it have been his duty to have reported that to the Comptroller immediately, or would he wait until he made out his regular report?

COUNSEL FOR DEFENDANT: He is calling for the conclusion of the witness as to what the bank examiner would do, whether he would send an immediate report or let it be reflected in his report.

THE COURT: The Court sustains the objection.

COUNSEL FOR COMPLAINANT: We except.

I have the ledger sheet of The Texas and Pacific Railway Company. I have it here from December 5, 1930, on down to the close of the bank.

The balance of The Texas and Pacific Railway Company on deposit at The First National Bank on January 29, 1931, was $22,264.10, as reflected by the ledger sheet. I have just been handed this list. I have not had an opportunity to check it over, but I assume it is correct. Including January 29, 1931, to August 5, 1931, inclusive, total of all deposits in that period are $132,220.27. The total deposits from August 6, 1931, to September 3, 1931, inclusive, were $16,545.48. The balance at close of business on August 6, 1931, was $50,428.10. At close of business on September 3, 1931, the balance was $54,325.90. The balance they had to start with, plus the deposits, minus the checks, would give the balance they had when the bank closed.

I have not read the agreed statement of facts in this case, but the balance was $54,325.90 at the close of business September 3rd. We added after the bank closed, for the purpose of allowing claim we added interest accrued up to the time, $30.84, and gave the claim for $54,356.74.

COUNSEL FOR COMPLAINANT: I believe there was one check for something like $310.00 that brought it up to the total as shown in the statement of facts.

COUNSEL FOR DEFENDANT: $54,646.94.

The list of Daily deposits referred to by the witness was introduced in evidence by Complainant, same was marked "C-2", and is as follows:

C-2

	132,220.27 s
8-6	30.00
	315.51
	356.30
8-7	198.79
	277.53
8-8	15.45
	450.00
	89.15
	230.20
8-10	613.15
	355.00
8-11	20.56
	165.00
	1,647.85
8-12	312.00
	128.80
8-13	148.95

	173.48
	60.00
8-14	155.53
	546.13
8-15	50.16
	865.39
	74.85
8-17	21.00
	868.35
	636.75
8-18	313.70
	292.23
8-19	238.47
	141.41
8-20	205.85
	277.00
8-21	151.61
	194.70
8-22	30.00
	40.00
	106.29
8-24	309.03
	290.00
8-25	224.75
	184.47
	90.00
8-26	210.12
	168.34
	490.00
	224.78
8-27	17.00
	216.00
	197.02
	125.00
8-28	228.09

	291.20
	175.00
8-29	516.72
	189.60
8-30	20.00
Int	88.92
8-31	307.42
	338.85
9-1	5.13
	99.44
	125.94
	100.00
9-2	33.65
	70.68
	30.00
9-3	75.39
	305.80

ON CROSS EXAMINATION:

This report of the examination made in August, 1931, was not sent in to the Comptroller of the Currency until after the bank closed. I know that of my own knowledge.

I have already allowed the claim of The Texas and Pacific Railway Company as an unsecured claim. I have a check, and have advised them they can have it at any time they want it, and they apparently don't want it; they haven't got it yet. Claim has been allowed and the check issued, the Receiver's check issued ready for delivery.

ON REDIRECT EXAMINATION:

Q That check may be delivered without prejudice to any rights claimed here by the plaintiff?

A We deliver the check in the usual manner as a dividend on a claim.

(Witness excused).

THE COMPLAINANT RESTED
THE DEFENDANT OFFERED NO TESTIMONY.

Argument of counsel for the respective parties was thereupon presented to the Court, and continued until 5:00 o'clock P. M., at which time Court recessed until 10:00 o'clock A. M. Thursday, May 26, 1932, and argument resumed; at the conclusion of which argument the Court found in favor of the Defendant and against the Complainant in said cause; also overruled motion to dismiss interposed by the defendant to the action of the complainant herein; and also overruled motion to strike of the Complainant on the cross action of the Defendant.

To which action of the Court in overruling Complainant's motion to strike or dismiss the cross bill of Defendant, and to the action of the Court in finding in favor of the Defendant and against Complainant herein, the Complainant then and there in open Court excepted.

BE IT FURTHER REMEMBERED, That on June 21, 1932, the Court made and filed Findings of Fact and Conclusions of Law as follows:

(Style and number of the case omitted).

FINDINGS OF FACT.

I

The Court adopts as paragraph I of the Findings of Fact in this case the Agreed Statement of Facts executed by the respective parties to this suit filed in this case on the 25th day of May, 1932; and the Court finds that the facts to be as stated in said Agreed Statement of Facts.

II

(a) The deposits of The Texas and Pacific Railway Company in The First National Bank of El Paso, prior to January 29, 1931, were fully protected and the repayment thereof by said bank to said railway company was fully guaranteed by two corporate surety bonds aggregating $50,000.00, to-wit: the first surety bond in the sum of $25,000.00 executed on August 7, 1924, by The First National Bank of El Paso, as principal, and the National Surety Company, as surety; and the second surety bond in the sum of $25,000.00 executed on April 25, 1927, by The First National Bank of El Paso, as principal, and Maryland Casualty Company, as surety. A copy of each of said surety bonds is attached to and made a part of the Agreed Statement of Facts adopted by the Court as Paragraph I hereof.

(b) During the month of January, 1931, and prior to the 29th day thereof, while said corporate surety bonds were in full force and effect, and while The First National Bank of El Paso was solvent and a going concern, the duly authorized active Vice President-Cashier of said bank called upon the President of The Texas and Pacific Railway Company at Dallas, Texas, and requested said railway officials to accept as security for The Texas and Pacific Railway Company's then deposits, and all future deposits or moneys to its credit in said bank, United States Government Liberty Loan Bonds of the par value of $50,000.00 in lieu of said corporate surety bonds. In explanation of this request said bank officer represented to said railway president that the First National Bank of El Paso had been required by The Texas and Pacific Railway to furnish it corporate surety bonds to secure its deposits in said bank, that the premiums on said bonds which had been paid by the bank were expensive and a

burden upon it and that The First National Bank of El Paso desired The Texas and Pacific Railway Company to accept said Liberty Bonds in lieu of said corporate surety bonds in order to relieve the bank from said premium payments.

(c) The president of the Texas and Pacific Railway Company advised said Vice President-Cashier of The First National Bank of El Paso that it was the policy of the railway company to require its depositories to provide ample and adequate security for its deposits, preferably corporate surety bonds; that under no circumstances would The Texas and Pacific Railway Company continue its account with and deposits in The First National Bank of El Paso without full and adequate security; that if the then outstanding corporate surety bonds were cancelled without the substitution of other adequate security acceptable to the railway company its account with said bank would be closed and its deposits withdrawn; but if the substitution of said liberty bonds, as proposed, would afford The Texas and Pacific Railway Company the same security as the then outstanding corporate surety bonds, said railway company would agree to such substitution solely for the purpose of enabling The First National Bank of El Paso to save the premiums on said corporate surety bonds.

(d) The said Vice President-Cashier of The First National Bank of El Paso advised the said president of The Texas and Pacific Railway Company that said liberty bonds, if and when substituted for said corporate surety bonds, would protect said railway company's deposits in said bank as fully and to the same extent as they were then protected by said corporate surety bonds and agreed to submit the proposed substitution plan to the attorneys for said bank for their investigation and ap-

proval. Said railway president, believing and relying upon said representations of said bank official, requested said Vice President-Cashier to have the officers and attorneys for said bank carefully investigate the proposed plan; and said railway president stated to said bank official that if, after such investigation, said bank officers and attorneys concluded that such substitution of liberty bonds in lieu of said corporate surety bonds would be legal and valid in every particular, would constitute and be a binding and enforceable obligation against said bank and would protect the railway company's deposits in said bank as fully and to the same extent as the then outstanding corporate surety bonds, The Texas and Pacific Railway Company would agree to such substitution and to the cancellation of said corporate surety bonds.

(e) The said Vice President-Cashier of The First National Bank of El Paso thereafter submitted the proposed substitution plan to the attorneys for said bank, and said attorneys, after investigating the same, advised the officers of said bank that such substitution could be legally made, would constitute and be in every respect a binding and enforceable obligation against The First National Bank of El Paso, and that said liberty bonds, if and when substituted for said corporate surety bonds would protect the deposits of The Texas and Pacific Railway Company as fully and to the same extent as said corporate surety bonds. At the request of the officers of said bank, the attorneys for the bank prepared the pledge agreement which was executed on January 29, 1931, in good faith, by The First National Bank of El Paso, acting by and through F. M. Murchison, its president and J. E. Benton, its cashier. Thereupon the liberty bonds enumerated in the Agreed Statement of Facts, adopted by the Court in paragraph I hereof (the par value of which aggregated $50,000.00), were placed in the Trust Department and

with the Trust Officer of The First National Bank of El Paso and in a separate envelope bearing the name of The Texas and Pacific Railway Company, to be held by said Trust Office separate and apart from all other securities of said bank in accordance with the terms of said pledge agreement. Said liberty bonds were thereafter and now are held separate and apart from all other securities of said bank and the liberty bonds for which plaintiff now sues are the identical liberty bonds which were placed in the hands of said Trust Officer on January 29, 1931. A full record of this transaction was made on the books of said bank on January 29, 1931, and said books ever since that date have reflected the same.

(f) The Vice President-Cashier of The First National Bank of El Paso sent the executed pledge agreement to the president of The Texas and Pacific Railway Company at Dallas, Texas, and advised said railway official that the officers and attorneys for said bank after carefully investigating the proposed substitution plan had concluded that the same would be in every respect a legal and binding obligation against said bank, that said executed pledge agreement had been prepared by the attorneys for the bank, and that the officers and attorneys for said bank were of the opinion and had declared that said executed pledge agreement and said liberty bonds, if and when substituted for said corporate surety bonds, would protect the deposits of The Texas and Pacific Railway Company in The First National Bank of El Paso as fully and to the same extent as said corporate surety bonds. Believing said representations of said bank official to be true, said railway president accepted said executed pledge agreement and said liberty bonds which had been placed in the custody of said Trust Officer of said bank in lieu of the then outstanding corporate surety bonds

and caused the latter to be cancelled as of January 30, 1931.

III

(a) After said liberty bonds had been substituted for said corporate surety bonds, The Texas and Pacific Railway Company, relying upon said pledge agreement and liberty bonds as security for its deposits, continued its account with and made deposits in The First National Bank of El Paso, and thereafter its average daily deposit balance in said bank substantially equalled the total par value of said liberty bonds.

(b) The Texas and Pacific Railway Company had on deposit with or to its credit in The First National Bank of El Paso on the following dates the sums shown below, to wit:

January 29, 1931	$22,264.10
August 6, 1931	50,428.10
September 3, 1931	54,646.94

(c) The Texas and Pacific Railway Company deposited in the First National Bank of El Paso from January 29, 1931, to August 5, 1931, inclusive, the total sum of $132,220.27.

(d) The Texas and Pacific Railway Company deposited in the First National Bank of El Paso from August 6, 1931, to September 3, 1931, inclusive, the total sum of $16,545.48.

(e) The total amount of $54,646.94 on deposit with or to the credit of The Texas and Pacific Railway Company in the First National Bank of El Paso on September 3, 1931, was moneys deposited by said railway company in said bank, subsequent to January 29, 1931, and/or accrued interest thereon, but said report was not

forwarded to the Comptroller's office until after the bank closed.

IV

(a) By substituting said liberty bonds as security for The Texas and Pacific Railway Company's deposits in lieu of said corporate surety bonds, The First National Bank of El Paso saved the premiums on said surety bonds, earned 4¼% interest on said liberty bonds and was able to hold the railway company's account which would have been closed had said corporate surety bonds been cancelled without other adequate security being furnished said railway company by said bank.

(b) The First National Bank of El Paso over a long period of years has furnished corporate surety bonds to protect the deposits of numerous private depositors.

(c) This was the first time the First National Bank had pledged its assets to secure a private deposit.

V

The Receiver of The First National Bank of El Paso has allowed as a general claim only the claim of The Texas and Pacific Railway Company as a secured depositor for the sum of $54,646.94 and has tendered to said railway company a first dividend check in the sum of $16,394.08, being 30% of the full amount of its claim.

VI

(a) The National Bank Examiners acting under the supervision and control of the Comptroller of the Currency made an examination of The First National Bank of El Paso commencing at 8 o'clock a. m. on August 6, 1931, and ending at noon on August 20, 1931, the report of said bank examiners to the Comptroller covering the

condition of said bank showed that liberty bonds of the par value of $50,000.00, were then pledged to secure the deposit of The Texas and Pacific Railway Company. This information was obtained from the books of the bank probably during the first two or three days of the examination.

(b) The officers of the First National Bank of El Paso were never notified or advised by either the bank examiners of the Comptroller of the Currency that the pledge of liberty bonds to secure the deposits of The Texas and Pacific Railway Company was either irregular, beyond the powers of the bank, or illegal, and no complaint of any character concerning the substitution agreement and the pledge of said liberty bonds was ever made to the officers of said bank or any of them by said bank examiners and/or the Comptroller of the Currency.

(Signed) CHARLES A. BOYNTON,
Judge.

O. K. T. HARDIE.
O. K. DEL W. HARRINGTON.
S. N. RUSSELL.

FILED June 21, 1932 (El Paso Division) D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas, by Flora L. Linker, Deputy Clerk.

(Style and number of case omitted).

CONCLUSIONS OF LAW.

I.

National banks in the United States have never had and do not now have express or implied power to pledge their assets to secure the payment of private deposits.

II.

The attempted pledge in this case of the Liberty bonds described in the Amended Bill of Complaint was one designed to secure the payment of a private deposit, and was and is wholly void, and of no effect.

III.

The attempted pledge of the securities in this case being void and contrary to law, and the public policy of the United States, the Plaintiff has never had and does not now have any valid liens or claims to, or rights in, the Liberty Bonds described in Plaintiff's Amended Bill of Complaint, and the Receiver is not estopped from asserting the invalidity of the attempted pledge of the bonds.

IV.

The Plaintiff has only an ordinary unsecured claim against the Receiver for the sum of $54,646.94, which claim has been already allowed by the Receiver, and upon which claim the Receiver has already offered to pay the regular dividends payable to ordinary depositors, and Plaintiff is therefore not entitled to any relief herein.

V.

The Defendant is entitled to have the pledge contract described in the amended Bill of Complaint declared invalid and of no effect, and to have Defendant's title to said bonds adjudged valid and free of all liens asserted by Plaintiff, and to have the cloud cast on Defendant's title to said Liberty Bonds by reason of Plaintiff's claims removed.

(Signed) CHARLES A. BOYNTON,
Judge.

FILED June 21, 1932, (El Paso Division), D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas, by Flora L. Linker, Deputy Clerk.

Based upon the foregoing Findings of Fact and Conclusions of Law, the Court entered Judgment in favor of Defendant herein; to which action of the Court the Complainant excepted.

Complainant filed exceptions to Conclusions of Law, as follows:

(Style and number of the case omitted).

PLAINTIFF'S EXCEPTIONS TO CONCLUSIONS OF LAW.

Comes now the plaintiff in the above numbered and entitled cause, counsel for defendant having submitted to counsel for plaintiff proposed conclusions of law to be submitted to the Court, and objects and excepts to such conclusions as so proposed, as follows:

(1) Plaintiff excepts to the conclusions of law as set out in Paragraph I and especially to that part thereof which holds "national banks in the United States have never had and do not now have express or implied power to pledge their assets to secure the payment of private deposits," because such finding is contrary to the plain terms of the statute granting the power to national banks to make contracts and to receive deposits.

(2) Plaintiff excepts to the conclusions of law as stated in Paragraph II to the effect that the pledge in this case of the liberty bonds described in the amended bill of complaint was and is wholly void and of no effect, because there is no law of the United States, stat-

utory or otherwise, prohibing national banks from making and entering into and performing the pledge agreement involved in this case.

(3) Plaintiff objects and excepts to Paragraph III of the conclusions of law, to the effect that plaintiff has never had and does not now have any valid liens or claims to, or rights in the liberty bonds described in plaintiff's amended bill of complaint, which conclusion is based upon the theory that the pledge agreement is void and contrary to law, because there is no law of the United States prohibiting the making, executing and performing of such pledge agreement or declaring the same void.

(4) Plaintiff excepts to the conclusion in Paragraph III, to the effect that plaintiff has never had and does not now have any valid lien, claim to or rights in the liberty bonds involved in this case, which conclusion is based upon the theory that said pledge agreement is contrary to the public policy of the United States, because there is no statutory declaration of the United States, and there is no decision of the Supreme Court of the United States nor or any Circuit Court of Appeals of the United States declaring such pledge agreement to be against the public policy of the United States.

(5) Plaintiff objects and excepts to the conclusions in Paragraph IV thereof, to the effect that plaintiff has only an ordinary unsecured claim against the Receiver for the sum of $54,646.94, because under the plain provisions of the pledge agreement, and the circumstances and conditions under which such money was deposited with and received by The First National Bank of El Paso, and the liberty bonds described in plaintiff's complaint placed in trust by said bank for plaintiff's use and benefit in the event said bank should fail to repay

to plaintiff the full amount of such deposit on demand, a valid lien was thereby created and now exists in plaintiff's favor on and against said liberty bonds to secure its said deposit; there being no law forbidding such agreement, plaintiff is entitled, at its option, either to the possession of said bonds or to have said lien foreclosed and said bonds sold and the proceeds arising from such sale, or so much thereof as may be necessary, applied to the extinguishment of plaintiff's said claim against defendant.

(6) Plaintiff further objects to the conclusions in Paragraph IV to the effect that plaintiff has only an ordinary unsecured claim against the Receiver for the sum of $54,646.94, because if it should be held that plaintiff is not entitled to the possession of said bonds or to the proceeds arising from the sale thereof, then under the provisions of said pledge agreement and the conditions under which such money was deposited by plaintiff in said The First National Bank of El Paso and the liberty bonds described in plaintiff's complaint were placed by said bank in trust for plaintiff's use and benefit to secure its said deposit, there being no law forbidding such agreement, plaintiff is entitled to recover the full amount of said deposit as for money had and received.

(7) Plaintiff further objects and excepts to the court's conclusion in said Paragraph IV, for the reason that if the court should be correct in holding the pledge of said liberty bonds void, the defendant cannot retain plaintiff's money deposited by virtue of said pledge contract and at the same time refuse to comply with its terms, and plaintiff is entitled to recover from defendant the full amount of its deposit in said bank at the time its doors were closed on September 4, 1931, with lawful interest thereon as for money had and received.

(8) Plaintiff further excepts to Paragraph IV of said conclusions of law, for the reason that under the circumstances and conditions which plaintiff's deposits were made in said bank, and of which there remains unpaid a balance of $54,646.94, the same became and were special deposits and under such circumstances and conditions plaintiff is entitled to recover the full amount thereof from defendant out of the funds of said bank.

(9) Plaintiff further excepts to Paragraph IV of the court's conclusions of law, for the reason that the pledge agreement under which the liberty bonds in this suit were placed in trust by said The First National Bank of El Paso to secure plaintiff's deposits is a matter of record in said bank, and it being admitted by defendant that the said records were examined by a duly authorized national bank examiner approximately thirty days before said bank was placed in the hands of the defendant as receiver, and that both said bank examiner and the Comptroller of the Currency ascertained and well knew from said examination that plaintiff's deposits in said bank were secured by said liberty bonds, and no complaint having been made to said bank either by such examiner or said Comptroller to the placing of said bonds as such security, both the defendant receiver and the Comptroller of the Currency, whom he represents, were and are estopped from asserting that said pledge is illegal.

(10) Plaintiff excepts to Paragraph V of said conclusions of law, wherein the court holds that defendant's title to said bonds should be adjudged valid and free of all liens asserted by plaintiff, because said pledge agreement is not forbidden by law and was fully executed in good faith by both parties, and said bonds were placed in trust and delivered by said bank to a trustee to be

held by him for the use and benefit of plaintiff and to be delivered by such trustee to plaintiff in the event said First National Bank of El Paso should fail to repay to plaintiff the full amount of its deposit upon demand; that demand having been made for such payment, and payment having been refused, plaintiff is entitled to have such bonds, or so many thereof as may be necessary to pay its said deposit, delivered to it by defendant.

(11) Plaintiff further excepts to Paragraph V of said conclusions of law, for the reason that if the court be correct in concluding that plaintiff is not entitled to the possession of said liberty bonds, that then plaintiff is entitled under said pledge agreement to have such bonds held in trust by defendant for its use and benefit until the full amount of plaintiff's said deposit has been paid to it by defendant.

(Signed) S. N. RUSSELL
D. W. HARRINGTON
M. E. CLIFTON
Attorneys for Plaintiff.

FILED June 21, 1932, (El Paso Division), D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas, by Flora L. Linker, Deputy Clerk.

The following order overruling plaintiff's exceptions was entered:

(Style and number of case omitted).

On this the 21st day of June, 1932, came on to be heard plaintiff's exceptions to the Court's conclusions of law in above numbered and entitled cause, said exceptions having been submitted to the Court in connection with the Court's proposed conclusions of law, and which proposed conclusions of law are now finally made by the Court.

And the Court having heard and considered said exceptions, and each and every thereof, and argument of counsel, and being fully advised in the premises, is of the opinion that neither of said exceptions is well taken; and it is therefore ordered that each and every of said exceptions be and the same is in all things hereby overruled.

To which action and ruling of the Court the plaintiff then and there in open court excepted.

(Signed) CHARLES A. BOYNTON
United State's District Judge.

O. K. T. HARDIE
O. K. DEL W. HARRINGTON
S. N. RUSSELL.

FILED June 21, 1932 (El Paso Division), D. H. Hart, Clerk, U. S. District Court, West. Dist. of Texas, by Flora L. Linker, Deputy Clerk.

SHORTHAND REPORTER'S CERTIFICATE.

* * * *

THE STATE OF TEXAS,
COUNTY OF EL PASO.

I, Roy Lassetter, Shorthand Reporter, hereby certify that the foregoing on 72 pages is a full, true and correct transcript of the evidence and bill of exceptions in the case of The Texas and Pacific Railway Company vs. S. O. Pottorff, Receiver of the First National Bank of El Paso, Texas, No. 251 Equity, El Paso Division of the United States District Court in and for the Western District of Texas.

Witness my hand at El Paso, Texas, this 5th day of July, A. D. 1932.

ROY LASSETTER,
Shorthand Reporter.

AGREEMENT OF COUNSEL.

* * * *

We, the undersigned attorneys of record for the respective parties, hereby agree that the foregoing record on 72 pages is a full, true and correct transcript of evidence and bill of exceptions in the case of The Texas and Pacific Railway Company vs. S. O. Pottorff, Receiver of The First National Bank of El Paso, No. 251 Equity, El Paso Division of the United States District Court in and for the Western District of Texas; and hereby approve the same as the transcript of evidence and bill of exceptions in said case.

Witness our hands this 5th day of July, A. D. 1932.

S. N. RUSSELL,
D. W. HARRINGTON,
M. E. CLINTON,
Attorneys for Complainant.

JONES, GOLDSTEIN, HARDIE & GRAMBLING,
THORNTON HARDIE,
Attorneys for Defendant.

APPROVAL OF THE COURT.

* * * *

The foregoing record having been approved by counsel for the respective parties to this case, and same having been examined and found correct, said record, on 72 pages, numbered from 1 to 72, is hereby approved as the statement of evidence and bill of exceptions in the case of The Texas and Pacific Railway Company vs. S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, No. 251 Equity, El Paso Division of the United States District Court in and for the Western

District of Texas; and ordered filed as a part of the record in said cause.

Witness my hand at Waco, Texas, this the 7th day of July, A. D. 1932.

CHARLES A. BOYNTON,
United States District Judge.

Filed July 7, 1932. D. H. Hart, Clerk, By T. H. Thompson, Deputy.

Stipulation with Reference to Liberty Bonds.

The parties to the above entitled and numbered cause, with the approval of the court, hereby stipulate as follows:

I

Pending the appeal of this cause and the final adjudication by the courts of the rights of the respective parties herein, the defendant, S. O. Pottorff, Receiver of The First National Bank of El Paso, agrees and obligates himself and his successors to hold those seven (7) certain United States Government Liberty Loan 4¼ Coupon Bonds, 1933-38, of the aggregate par value of $50,000.00, being the same liberty bonds described in the decree of the court entered in this cause and described by numbers as follows:

G00129907	$ 5,000.00
A00115901	5,000.00
E00040105	5,000.00
K00129870	5,000.00
G00353057	10,000.00
H00353058	10,000.00
H00298068	10,000.00

separate and apart from all assets of said bank, unless said liberty bonds are sold pursuant to Paragraph II hereof.

II

Plaintiff, The Texas and Pacific Railway Company, agrees and hereby authorizes said defendant, if he so desires, to sell said liberty bonds for cash for the highest price obtainable, and in no event for less than their par value, and in the event of such sale or sales said defendant hereby agrees and obligates himself and his successors to hold the proceeds therefrom, separate and apart from all assets of said bank expressly subject to and for the purpose of satisfying any and all liens, claims or judgments which the courts may adjudicate that The Texas and Pacific Railway Company has, or to which it may be entitled, in and to said liberty bonds or the proceeds from the sale or sales thereof.

III

Said defendant, S. O. Pottorff, hereby expressly agrees that the Court, in allowing the plaintiff an appeal in this cause, may enter an order suspending and superseding the decree of the Court entered herein on May 26, 1932, upon the plaintiff filing in said cause a bond in the sum of $1,000.00, which shall act both as a supersedeas and a bond for costs and damages on appeal.

IV

This stipulation shall be filed among the papers of this cause and shall constitute and be a part of the record thereof.

In witness whereof the parties hereto have signed this stipulation, by their attorneys, this the 12th day of August, 1932.

S. N. RUSSELL
D. W. HARRINGTON
M. E. CLINTON
Attorneys for Plaintiff.
JONES, GOLDSTEIN, HARDIE &

GRAMBLING
By THORNTON HARDIE
Attorneys for Defendant.

S. O. POTTORFF, Receiver
First National Bank,
El Paso, Texas.

The foregoing agreement is hereby approved this 12th day of August, A. D. 1932.

CHARLES A. BOYNTON,
District Judge.

Filed August 23, 1932 (El Paso Division) D. H. Hart, Clerk, U. S District Court, West. Dist. of Texas, By Flora L. Linker, Deputy Clerk.

Petition for Appeal.

To the Honorable Charles A. Boynton, District Judge:

The above named plaintiff, The Texas and Pacific Railway Company, feeling aggrieved by the decree rendered and entered in the above entitled cause on the 26th day of May, 1932, does hereby appeal from said decree to the Unitetd States Circuit Court of Appeals for the Fifth Circuit at New Orleans, Louisiana, for the reasons set forth in the Assignment of Errors filed herewith, and prays that its appeal be allowed and that citation be issued as required by law, and that a transcript of record, proceedings and papers upon which said decree was based, duly authenticated, be sent to the United States Circuit Court of Appeals for the Fifth Circuit under the rules of such court in such cases made and provided.

And your petitioner further prays that the decree of the court should be suspended and superseded, and that the court enter the proper order with reference to the

security to be required to perfect this appeal, and to supersede the judgment of the court.

S. N. RUSSELL
D. W. HARRINGTON
M. E. CLINTON
Attorneys for Plaintiff.

Order Allowing Appeal.

On motion of the plaintiff it is hereby ordered that the appeal of the plaintiff from the judgment of this court to the United States Circuit Court of Appeals for the Fifth Circuit at New Orleans, Louisiana, be and the same is hereby allowed, and that a certified transcript of the record, testimony, exhibits, stipulations and other proceedings in this cause be forthwith transmitted to said Circuit Court of Appeals.

It is further ordered that the judgment of the court in this cause be suspended and superseded in accordance with the stipulation of the parties filed herein, upon the plaintiff filing a bond in the penal sum of One Thousand ($1,000.00) Dollars, to be conditioned as provided by law, such bond to act both as a supersedeas and as a bond for costs and damages on appeal.

Done this 23rd day of August, 1932.

CHARLES A. BOYNTON,
District Judge.

Waiver of Citation.

Copy of the above order received, and citation on appeal waived, this 23rd day of August, 1932.

JONES, GOLDSTEIN, HARDIE & GRAMBLING,

By T. HARDIE

Attorneys for Defendant.

Filed, U. S. District Court, Western District of Texas, Aug. 23, 1932. D. H. Hart, Clerk, By J. N. Phillips, Deputy.

Assignment of Errors.

Comes now the Texas and Pacific Railway Company, plaintiff in the above styled and numbered cause, and files the following assignments of error upon which it will rely in the prosecution of its appeal herewith petitioned for in said cause from the decree of this Court entered therein on the 26th day of May, 1932.

I

The trial court erred in overruling and in not granting plaintiff's motion to dismiss defendant's cross-bill.

II

The trial court erred in denying the relief prayed for by plaintiff.

III

The trial court erred in concluding and in holding in paragraph I of its Conclusions of Law that "National banks in the United States have never had and do not now have express or implied power to pledge their assets to secure the payment of private deposits."

IV

The trial court erred in concluding and in holding in paragraph II of its Conclusions of Law that "the pledge of the Liberty Bonds described in the Amended Bill of Complaint was one designed to secure the payment of a private deposit."

V

The trial court erred in concluding in paragraph II of its Conclusions of Law and in decreeing that the pledge in this case of the Liberty Bonds described in the Amended Bill of Complaint was and is wholly void and of no effect.

VI

The trial court erred in concluding and in holding in paragraph III of its Conclusions of Law that the pledge of the securities in this case was and is contrary to law.

VII

The trial court erred in concluding and in holding in paragraph III of its Conclusions of Law that the pledge of the securities in this case was and is contrary to the public policy of the United States.

VIII

The trial court erred in concluding and in holding in paragraph III of its Conclusions of Law that "plaintiff has never had and does not now have any valid liens or claims to, or rights in, the Liberty Bonds described in Plaintiff's Amended Bill of Complaint."

IX

The trial court erred in concluding and in holding in paragraph III of its Conclusions of Law that "The Receiver is not estopped from asserting the invalidity of the attempted pledge of the bonds."

X

The trial court erred in concluding and in holding in paragraph IV of its Conclusions of Law that "Plaintiff has only an ordinary unsecured claim against the Re-

ceiver for the sum of $54,64[illegible]4 * * * , and Plaintiff is therefore not entitled to any relief herein."

XI

The trial court erred in overruling each of plaintiff's exceptions respectively to the court's Conclusions of Law, which exceptions are numbered from I to XI, inclusive.

XII

The trial court erred in concluding and in holding in effect as a matter of law that plaintiff's deposits in The First National Bank of El Paso were general deposits, that they became assets of said bank and as such passed to the defendant Receiver to be distributed by him among the general creditors of said bank.

XIII

The trial court erred in decreeing "that said liberty bonds are the property of the defendant, constituting assets of his trust, to be administered by him for the benefit of the general creditors of The First National Bank of El Paso."

XIV

The trial court erred in concluding and in holding, in effect, as a matter of law that plaintiff's deposits in The First National Bank of El Paso were not, or did not become, and are not now special deposits, the title to which remained and now is in plaintiff, and that they are not now held by said Receiver in trust for the use and benefit of The Texas and Pacific Railway Company.

XV

The trial court erred in concluding and in holding, in effect, as a matter of law, that the payment by defendant Receiver to plaintiff of the full amount of its claim

would constitute and be an unlawful preference prohibited by the national banking act.

XVI

The trial court erred in concluding and in holding, in effect, as a matter of law, that plaintiff is not entitled to recover of and from said Receiver, as for money had and received, the full amount of its deposits in The First National Bank of El Paso, and lawful interest thereon from the 4th day of September, 1931, until paid.

XVII

The trial court erred in concluding and in holding, in effect, as a matter of law that the knowledge of the bank examiners of said pledge agreement was not the knowledge of the Comptroller of the Currency and that said Comptroller had no notice, actual or constructive, of said pledge agreement until after said bank had closed its doors.

XVIII

The trial court erred in concluding and in holding, in effect, as a matter of law that the defendant Receiver is not estopped from asserting that plaintiff is not entitled to a lien upon said liberty bonds or to a lien upon the funds in the possession of said Receiver.

XIX

The trial court erred in concluding and in holding, in effect, as a matter of law, that the national bank examiners, who examined The First National Bank of El Paso early in August, 1931, and who discovered on the books of said bank the record of the pledge agreement, were under no legal obligation, if said pledge agreement was irregular and unlawful, to demand of the officers of said bank the cancellation of said pledge agreement; and

that said bank examiners were under no legal obligation to immediately notify the Comptroller of the Currency of the alleged irregular and unlawful pledge without waiting to complete and mail their final report of such examination to said Comptroller.

XX

The trial court erred in decreeing "that any cloud existing on defendant's title to said liberty bonds by reason of the above mentioned (pledge) contract, and by reason of the assertion of any claims to said bonds by plaintiff be, and the same is hereby removed."

XXI

The trial court erred in decreeing "that the plaintiff, The Texas and Pacific Railway Company, is not entitled to have or recover any relief herein against the defendant, S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas," and in further decreeing "that Plaintiff, The Texas and Pacific Railway Company, take nothing by this suit."

XXII

The trial court erred in decreeing "that as to plaintiff's suit the defendant recover of and from plaintiff all costs in this behalf incurred."

XXIII

The trial court erred in decreeing "That the plaintiff, The Texas and Pacific Railway Company, desist from asserting any further rights or claims in said liberty bonds."

XXIV

The trial court erred in concluding and in holding in effect as a matter of law that the failure of the vice-

president-cashier of The First National Bank of El Paso to advise the president of The Texas and Pacific Railway Company that the Maryland Casualty Company had notified the officers of the bank that said surety company was going off all surety bonds was not constructive fraud or a fraud in law upon the railway company under the facts of this case.

WHEREFORE, plaintiff presents these assignments of error with its petition for allowance of appeal herein, and prays for citation as provided by law, and that the decree of the trial court be reversed, and for such other and further relief as to the Court may seem just and proper.

S. N. RUSSELL
D. W. HARRINGTON
M. E. CLINTON
Attorneys for Plaintiff, The Texas and Pacific Railway Company.

Filed, U. S. District Court, Western District of Texas, Aug. 23, 1932, D. H. Hart, Clerk, By J. N. Phillips, Deputy Clerk.

Supersedeas Bond.

KNOW ALL MEN BY THESE PRESENTS, That we, The Texas and Pacific Railway Company, as principal, and the other signers hereto as sureties, are held and firmly bound unto S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, in the full and just sum of One Thousand ($1,000.00) Dollars, to be paid to the said S. O. Pottorff, Receiver, and his successors, to which payment well and truly to be made we bind ourselves, our assigns, successors, heirs, executors and administrators, jointly and severally by these presents:

The condition of this bond is such, however, that WHEREAS at the April 1932 Term of the above court, in a suit pending in said court between the above named plaintiff and defendant, a judgment was rendered against the plaintiff in favor of the defendant, and said The Texas and Pacific Railway Company has appealed from said judgment to the United States Circuit Court of Appeals for the Fifth Circuit in an effort to reverse and set aside the judgment of the court rendered in this cause.

NOW THEREFORE, if said The Texas and Pacific Railway Company shall prosecute its said appeal to effect, and pay and satisfy all damages and costs if it shall fail to prevail in its appeal, then this obligation shall be void, otherwise to remain in full force and effect.

Executed this 23rd day of August, 1932.

THE TEXAS AND PACIFIC RAIL-
RAILWAY COMPANY,
Principal,
By S. N. RUSSELL,
Its Attorney of Record.

R. W. McAFEE
C. N. BASSETT
Sureties.

The sureties on the foregoing bond are considered sufficient thereto by me.

J. N. PHILLIPS,
Deputy Clerk.

The within bond is hereby approved both as to its sufficiency and as to its form, this 23rd day of August, 1932.

CHARLES A. BOYNTON,
District Judge.

Notice of filing of the foregoing bond is hereby waived.

JONES, GOLDSTEIN, HARDIE &
GRAMBLING,
By T. HARDIE
Attorneys for S. O. Pottorff,
Receiver.

Filed, U. S. District Court, Western District of Texas, Aug. 23, 1932, D. H. Hart, Clerk, By J. N. Phillips, Deputy Clerk.

Bill of Costs.

CLERK'S FEES, ETC.

Instituting suit	$ 5.00
Filing Defendant's Motion to Dismiss	5.00
Filing and entering Judgment	5.00
Filing Petition for Appeal	5.00
Comparing, indexing and certifying printed Transcript of Record	24.50
Cost of printing record	122.00

MARSHAL'S FEES

Serving original subpoena	2.00

REPORTER'S FEE

Per diems	20.00

NOTARY'S FEE

Taking one deposition	10.00

Praecipe for Transcript of Record.

To D. H. Hart, Esq., Clerk of the above Court:

You are hereby requested to make a transcript of record in this case, under the rules of this court, to be filed in the United States Circuit Court of Appeals for the Fifth Circuit, pursuant to an appeal allowed in the above

entitled cause, and to include in such transcript of record the following pleadings, proceedings and documents, to-wit:

1. Index.
2. Caption.
3. Plaintiff's First Amended Bill of Complaint.
4. Motion of S. O. Pottorff to dismiss Plaintiff's Amended Bill of Complaint, filed May 25, 1932.
5. Cross-bill of S. O. Pottorff, Receiver, filed April 5, 1932.
6. Answer of S. O. Pottorff to Plaintiff's Amended Bill of Complaint, filed May 25, 1932.
7. Motion of plaintiff to dismiss cross-bill of S. O. Pottorff, filed May 18, 1932.
8. Court's oral findings.
9. Judgment.
10. Findings of fact and conclusions of law.
11. Plaintiff's objections and exceptions to conclusions of law.
12. Order overruling plaintiff's objections to conclusions of law, with plaintiff's exceptions to action of the court in overruling same,
13. Statement of evidence and bill of exceptions.
14. Stipulation with reference to defendant holding liberty bonds involved, or proceeds of sale thereof, pending appeal and subject to final judgment.
15. Petition for appeal and for fixing amount of security to perfect appeal.
16. Assignments of error.
17. Order allowing appeal and fixing amount of security to perfect.
18. Supersedeas bond, with court's approval.
19. Cost bill, including cost for preparing transcript of record.
20. This praecipe for transcript of record.

21. Clerk's certificate.

S. N. RUSSELL
D. W. HARRINGTON
M. E. CLINTON
Attorneys for The Texas and Pacific Railway Company.

Due and legal service of the foregoing praecipe is hereby acknowledged, and it is agreed that the foregoing shall constitute the transcript of record.

Executed this 23rd day of August, A. D. 1932.

JONES, GOLDSTEIN, HARDIE & GRAMBLING,
By T. HARDIE,
Attorneys for S. O. Pottorff, Receiver.

Filed, U. S. District Court, Western District of Texas, Aug. 23, 1932, D. H. Hart, Clerk, By J. N. Phillips, Deputy Clerk.

Clerk's Certificate.

I, D. H. Hart, Clerk of the United States District Court for the Western District of Texas, hereby certify that the foregoing, on 117 pages, is a true and correct transcript of the proceedings had and the orders entered in cause No. 251 in Equity, styled The Texas and Pacific Railway Company vs. S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, as the same appear on file and of record in this office.

And I do further certify that the foregoing transcript embraces only such instruments and orders as are specified in the praecipe filed by the appellant and agreed to by the appellee.

Witness my official signature and the seal of said court hereto affixed at office in the City of El Paso, Texas, this 8th day of September, A. D. 1932.

D. H. HART, *Clerk,*

(SEAL) By.....*Deputy Clerk.*

J. N. PHILLIPS.

Minute entry of submission, November 9, 1933, omitted in printing.

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 6748

THE TEXAS & PACIFIC RAILWAY COMPANY, Appellant,

versus

S. O. POTTORFF, Receiver of the First National Bank of El Paso, Texas, Appellee

Appeal from the District Court of the United States for the Western District of Texas

(January 19, 1933)

Before Bryan, Foster and Hutcheson, Circuit Judges

OPINION OF THE COURT—Filed January 19, 1933

HUTCHESON, Circuit Judge:

This case, and the case just decided, Pottorff, Receiver, v. El Paso-Hudspeth Counties Road District of Texas, — Fed. (2) —, involving the validity and the enforceability against the receiver of a contract of the bank pledging some of its assets to secure a depositor, in the one case of private, in the other of public funds, are companion cases. They were tried in the same court at the same time.

Appellee urged in the court below, and urges here, in each of the cases, that the agreement under which the securities were pledged is invalid and unenforceable as beyond the power of the bank and in contravention of public policy. The District Judge disagreeing with the receiver in the Road District case, agreed with him in this one. Following B. & O. v. Smith, 56 Fed. (2) 799, he thought that the authority which he had held under applicable statutes the bank had to secure deposits of public did not exist in the absence of statute to secure deposits of private funds; that the agreement was beyond the power

of the bank to make and void, and that plaintiff could not enforce it.

The facts in this case, as in the other, are undisputed. At the time the bank failed, appellant had on deposit $54,646.94. The receiver has approved its claim for that sum and has tendered a dividend on account of it of $16,394.08. He has refused to surrender the Liberty Bonds put up to secure the deposit. These are the circumstances of their pledging.

In July, 1922, the railway being then in receivership, the First National Bank of El Paso was designated as an additional depository upon condition that it should furnish bonds with good, solvent sureties. Thereafter the deposits first of the receiver, later of the company, were fully protected and their repayment guaranteed by corporate surety bonds. On January 29, 1931, the bank being still a solvent, going concern, the railway was induced by the bank to permit it to substitute for the surety bonds theretofore securing the deposit the Liberty Loan bonds in question. They were deposited with the trust officer of the bank to be held as security for the repayment, upon demand, of the deposits. By the agreement the bank saved bond premiums and secured the continuance of the deposit account, carrying an average balance of $50,000 which, but for its being secured either by bonds or pledge would have been withdrawn.

The record shows that though the bank had over a long period of years with the acquiescence of the Banking Department, furnished corporate surety bonds to protect the deposits of numerous private depositors, this was the first instance of its pledging assets to secure private funds. Further, the record is not only devoid of affirmative proof that the thing the bank did here accords with national banking practices and customs, or is at all a necessary or desirable practice, but no single other instance of the practice having been indulged in has been presented, and it shows that with the same uniformity which has attended the recognition of the power of national banks to secure public deposits by pledge, the Comptroller has ruled that they may not do so in the case of private deposits.

The general questions of the power of banks, state and national, in the absence of statutory authority, to pledge their assets to secure deposits, and of the enforceability of

such pledges when made, are interesting ones and have been the subject of many decisions. Raised usually in cases involving pledges to secure public deposits, and usually with reference to state banks, the questions have been differently decided in different jurisdictions, under the influence of different statutes and different views of the public policy involved. None of the cases, except arguendo, as in B. &, O. v. Smith supra, also 48 Fed. (2) 861; Schumacher vs. Eastern, 52 Fed. (2) 925; Sneedon v. City of Marion, 58 Fed. (2) 341, have drawn any distinction between private and public deposits as such, as to the power to secure them; but the question of power or not, where it had not been expressly conferred, has been decided broadly under the influence of the view taken by the particular court in the light of the existence or non-existence of statutes as to whether it accorded with public policy to imply the power. In jurisdictions where the courts have held that to permit one depositor to thus gain a preference over another, is contrary to sound public policy, they have stricken down pledges without regard to whether the funds secured were public or private, while in one or two jurisdictions where no contravention of public policy in thus pledging assets is seen, the courts have without distinction between them, sustained pledges of private and public deposits.[1]

In most of the cases this controversy has arisen where though there was statutory authority for pledging assets of a designated kind to secure public deposits, the statute did not expressly authorize the particular pledging. In those cases the question argued has been whether statutes authorizing pledging must, as contrary to a broad public policy, be construed strictly as enabling only in the very terms, or liberally, as effective analogically; whether they must be regarded as declaring a narrow or a broad public policy in regard to the pledging of assets to secure public deposits. An examination of these cases will show at once how great an influence on the decisions has been exerted by the varying views of public policy entertained by the

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[1] NOTE 1. Able v. Rhoads, 84 Pa. 319; Ward v. Johnson, 95 Ill. 215 cited in the text of Morse on Banks & Banking, 6 Ed., Vol. 1, sec. 63, p. 182, as holding that banks may secure persons who loan it money by deposits.

courts, and how uncertain, wavering and unreliable a guide, unless fixed by statute, this same public policy is. Twin City Pipe Line v. Harding, 283 U. S. 363; Ireland v. Craggs, 56 Fed. (2) 785. It will disclose that what is heresy in one jurisdiction, is doctrine in another, and even sometimes that what is heresy in one court in the same jurisdiction is doctrine in another court there.[2] It will show that most of the reasoning of the courts is that kind of rationalization where logic serves desire by bringing forth conclusions which the premises were assumed to secure. It will completely explain the apparent contradictions in the holdings. Cases taking the view that public policy requires statutes authorizing the giving of security for deposits to be strictly construed, and that the statutes in their precise terms are the measures of the banks' powers, are Commercial Bank & Tr. Co. v. Citizens Bank & Guaranty Co. (Ky.), 45 L. R. A. (N. S.) 950; Foster v. City of Longview (Tex.), 26 S. W. (2) 1059; Austin v. Lamar Co. (Tex.), 26 S. W. 1062; Farmers & Merchants v. Con. School Dist. (Minn.), 290 N. W. 163; Bliss v. Pathfinder (Neb.), 240 N. W. 291 (but see Bliss v. Marion, 237 N. W. 682); Shorneck v. Butler, 172 N. E. 181. Cases, and these are supported, we think, by the better reasons, holding that where the Legislature of a state has declared in specific statutes that deposits of public money must be secured this sufficiently indicates the public policy of the state toward the securing of public deposits, to sustain contracts whether in exact accordance with the statute or not, made in good faith for their security are, Am. Bank & Trust Co. v. Palm Beach (Fla.), 117 So. 900; 67 A. L. R. 1400; McLane v. Hunker, 299 Pac. 1075; Cameron v. Christy, 133 Atl. 551; McPherson v. Nat. Surety Co., 212 Pac. 489, c/f Michie Banks & Banking, Vol. 4, p. 22, sec. 19.

A few of the cases have put their decision against the power firmly on the ground that no express power to pledge assets to secure deposits having been granted to a bank, no basis in the absence of a statute authorizing or requiring the giving of security exists for the implication of the power. Those cases which have sustained the power

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[2] NOTE 2. Foster v. Longview, 11 S. W. (2) 217; 26 S. W. (2) 1059; Austin v. Lamar Co., 11 S. W. (2) 553; 26 S. W. 1062.

of a bank to pledge, by implying it, find support for that holding in the view that a deposit is a loan and claim to find in the established law that a bank has implied power to borrow money and pledge its assets authority to take deposits for such a pledge. Those denying the implication of the power do so on the ground that though a deposit does make the bank a debtor to the depositor, it is not a loan. They insist that the power must be sought elsewhere than in the implied power to make loans.

Few cases have arisen in the state courts, and only one in the national courts, B. & O. v. Smith, supra, has been called to our attention where the pledge has been made to a private depositor. These cases, except the two referred to in the preceding Note One have held against the power. None of them have pitched the holding on the private character of the deposit. In some the existence of a statute containing a general prohibition against the giving of security has compelled the decision, Porter v. Canyon Co. Fire Ins. Co., 263 Pac. 632. In some, as in Carter v. Brock (La.), 110 So. 71, though the court has declared against the power this has been dicta, for the actual holding was that the transaction was valid as not a deposit but a loan. McCown v. Edwards (Ark.), 48 S. W. 558, is a clear case distinguishing a deposit from a loan, and upon that distinction holding invalid the pledge of assets to secure a private deposit. In that case a guardian authorized to loan the money of his ward put it on general deposit upon the security of a pledge. In a suit to charge him upon failure of the bank he was held liable, the court saying "There is a vital distinction between a loan to a bank and a deposit with a bank. In one case security may be and usually is exacted; in the other, security may not be given by the bank. The power of the bank to borrow money and give security for it is unquestioned, while the power of the bank to give security for an ordinary deposit has been expressly denied."

We agree with this view that a deposit does indeed create a debt, but it creates something more. That a deposit is one thing, a loan another. "The striking fact is that a real difference between a deposit and a loan has always been assumed as a matter of custom in the banking business itself, and in Legislatures dealing with the subject." Divide Co. v. Baird, 212 N. W. 236.

We therefore reject the view that implied authority to pledge assets as security for loans extends to pledging them to secure deposits. We agree also with the view expressed, that generally speaking a bank's general powers do not authorize it to pledge assets for deposits. Michie, supra. We find specifically that this bank had no such power, and this not because the recognition of the power would conflict with our views of public policy, but because no express power to do so has been conferred upon it by statute, and because not only does the record not support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank, but the judicial knowledge of banking practices and customs which we may take establishes the contrary to be true.

It remains only to inquire whether, though the contract is ultra vires, the railway can enforce its claim on the pledged bonds on the ground that though the agreement was beyond its powers, the bank has, by making it, obtained the deposit and therefore may not keep the bonds without returning the deposit made on the faith of their pledging.

Appellant argues that having complied with its part of the agreement by leaving its funds on general deposit with the bank, the bank ought to be made to do what it promised, that is, devote the securities to making appellant whole. It argues (1) that though the bank's agreement be ultra vires, estoppel prevents it saying so. (2) That the contract for depositing was a single one, the agreement for deposit being precedently conditioned on the agreement for security, and that agreement failing, the bank holds the funds not as debtor for a general depositor, but as trustee for a special one.

We cannot agree with either of these contentions. It is perfectly clear that though the Railway Company was induced by the promise of security to deposit its funds, there are two agreements here, not one. One, that the bank should pay back to the railway upon demand the sums deposited with it as other general deposits were. This entirely valid contract the receiver has recognized, and has offered to pay the Railway a dividend on account of it. The other is an agreement for security. This we have found to be in-

valid and without contractual force as beyond the corporate powers. This agreement plaintiff asks the aid of this Court to enforce.

It is settled law in the courts of the United States that what a corporation cannot bind itself to do, the courts will not compel. California Nat. Bank v. Kennedy, 167 U. S. 362; Union Pac. Ry. v. Chicago, 163 U. S. 564; Central Transportation Co. v. Pullman Car Co., 139 U. S. 60. Especially will it not do it in a case of this kind, where the controversy is not between the bank and the railway, but between the railway and the bank's creditors, the bank having failed, and "the interest of others than the parties," Beasley v. T. & P., 191 U. S. 492, being involved.

This is not a case like Aldrich v. Chemical Nat. Bank, 176 U. S. 636; Citizens Nat. Bank vs. Appleton, 216 U. S. 206; Schneider v. Thompson, 58 Fed. (2) 98, of a solvent bank which has obtained the benefit of a transaction, seeking to avoid, on the ground of ultra vires, returning what it has received. In those cases the suit was not on the contract, but on the benefits received. This is not such a case. It is upon a contract, to enforce it.

Appellant's claim that if it cannot have its contract, money of the bank, to the extent of its deposits, should be now earmarked and held in trust for it, is equally without merit. In the first place, while it is certainly true that parties may by agreement, give to deposits which would otherwise be general, the special character of trust funds, an agreement definitely fixing the character of the deposit as general may not be disregarded because, if the depositor had fully known the law and the facts, he would have acted differently for his protection. Fagan v. Whiddon, 57 Fed. (2) 631.

Appellant's contract with the bank for the repayment of its deposits on demand was valid. These deposits it can have back, if the bank can pay. The contract for security was indeed invalid, but there is no basis at all here for declaring a trust. Here is a contract for depositing, which was valid, and one for security which was invalid because of want of power in the bank, of which want of power appellant was as fully charged with knowledge as the bank was. The result is simply that though the railway has the right to press its claim for its debt, it cannot do so for the security.

It cannot be that a general depositor in a bank, who has made an agreement for security, may, because the security fails through an invalidity, which in law it knew, find the bank converted into a trustee and himself a cestui que trust of the money of the bank to the extent of the amount of his general deposit.

The judgment is affirmed.

IN UNITED STATES CIRCUIT COURT OF APPEALS

No. 6748

THE TEXAS & PACIFIC RAILWAY COMPANY,

versus

S. O. POTTORFF, Receiver of the First National Bank of El Paso, Texas

JUDGMENT—January 19, 1933

This cause came on to be heard on the transcript of the record from the District Court of the United States for the Western District of Texas, and was submitted to the Court upon the record and briefs on file;

On consideration whereof, It is now here ordered, adjudged and decreed by this Court, that the judgment of the said District Court in this cause be, and the same is hereby, affirmed;

It is further ordered, adjudged and decreed that the appellant, The Texas & Pacific Railway Company, and the sureties on the appeal bond herein, R. W. McAfee and C. N. Bassett, be condemned, in solido, to pay the costs of this cause in this Court, for which execution may be issued out of the said District Court.

IN UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

ORDER EXTENDING TIME TO FILE PETITION FOR REHEARING—
February 9, 1933

On this the 9 day of February, 1933, came on to be heard the motion of appellant, The Texas & Pacific Railway Company, for an additional thirty days in which to prepare, file and present its petition for rehearing in the above styled cause, and it appearing to the Court that said motion should in all things be granted,

It is therefore ordered that appellant be and it hereby is granted twenty days in addition to the twenty-one days allowed by the rules of this Court in which to prepare, file and present its petition for rehearing in this cause.

(Signed) J. C. Hutcheson, Jr., U. S. Circuit Judge.

No. 6748

UNITED STATES CIRCUIT COURT OF APPEALS
FIFTH CIRCUIT

THE TEXAS AND PACIFIC RAILWAY COMPANY,

Appellant,

v.

S. O. POTTORFF, RECEIVER OF THE FIRST NATIONAL BANK OF EL PASO, TEXAS,

Appellee.

Appeal From the United States District Court for the Western District of Texas, El Paso Division

APPELLANT'S PETITION FOR REHEARING

To the Honorable United States Circuit Court of Appeals for the Fifth Circuit:

Comes now the Texas and Pacific Railway Company, appellant in the above entitled and numbered cause, and respectfully moves and prays the Court to grant it a rehearing in this cause and for grounds of this petition would show:

I

The Court erred in overruling and in not sustaining appellant's first specification of error and its point one thereunder reading as follows:

> "The trial court erred in concluding and in holding as a matter of law that the bank's pledge of liberty bonds to secure the railway company's deposit was wholly void and of no effect" (Brief, p. 18).
>
> "The First National Bank of El Paso acted within its lawful authority when it pledged its liberty bonds to secure the repayment of The Texas and Pacific Railway Company's deposit" (Brief, p. 21).

II

The Court erred in its findings that the record is "devoid of affirmative proof that the thing the bank did here accords with national banking practices and customs, or is at all a necessary or desirable practice" and that "no single other instance of the practice having been indulged in has been presented" (Opinion, p. 3), because the record shows that the pledge agreement enabled the bank to save the premiums on two corporate surety bonds, to earn 4 1/4 per cent on the pledged liberty bonds, and to hold the railway company's deposit (Tr. 94); and appellant's brief, page 31, calls attention to at least one other instance in which a national bank has pledged its

assets to secure the deposit of a railway company. Baltimore & Ohio Railroad Company v. Smith, 56 Fed. (2d) 799.

III

The Court erred in its conclusion that the record does not "support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" (Opinion, p. 7), because the record shows that the pledge agreement enabled the bank to save the premiums on two corporate surety bonds, to earn 4 1/4 per cent interest on the pledged liberty bonds, and to hold the railway company's deposit (Tr. 94).

IV

The Court erred in its finding and conclusion that the record "shows that with the same uniformity which has attended the recognition of the power of national banks to secure public deposits by pledge, the Comptroller has ruled that they may not do so in the case of private deposits" (Opinions, p. 3), because such finding and conclusion finds no support in the record which shows that the comptroller of the currency never made any com-

plaint to the officers of the First National, although his bank examiners learned of the pledge agreement about August 8, 1931, nearly one month before the bank closed (Tr. 94-95).

V

The Court erred in holding that "the judicial knowledge of banking practices and customs which we may take establishes" that the giving of pledges for private deposits is not a reasonable incident to the business of receiving deposits and is not necessary to the proper conduct of the business of a national bank; and the Court further erred in basing its decision adverse to appellant in part upon such judicial knowledge (Opinion, p. 7), for the reasons assigned under the foregoing third ground of error.

VI

The Court erred in its holding that "a deposit is one thing, a loan another", and in rejecting "the view that implied authority to pledge assets as security for loans extends to pledging them to secure deposits" (Opinion, p. 7).

VII

The Court erred in holding that "generally speaking a bank's general powers do not authorize it to pledge as-

sets for deposits", that the contract for security "was invalid because of want of power in the bank", that "this bank had no such power * * * because no express power to do so has been conferred upon it by statute", and because the record does not "support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" (Opinion, pp. 7, 9), for the reasons assigned under the foregoing third ground of error.

VIII

The Court placed too heavy a burden of proof upon appellant and particularly erred in holding, in effect, that to sustain the bank's implied power to make the pledge agreement, appellant must affirmatively prove that such agreement was "necessary to the proper conduct of the business of a national bank" and "accords with national banking practices and customs" (Opinion, pp. 3, 7).

IX

The Court erred in holding that appellant "was as fully charged with knowledge as the bank was" of the latter's "want of power" to make the contract for security (Opinion, p. 9), such power being dependent in

part upon the needs of the bank or what might be useful or beneficial to it.

X

The Court erred in overruling and in not sustaining appellant's second specification of error and its point two thereunder reading as follows:

> "The trial court erred in concluding and in holding as a matter of law that the receiver is not estopped from asserting the invalidity of the pledge agreement without returning or tendering back to the railway company the full amount of its deposits". (Brief, p. 18).
>
> "The receiver is estopped to assert the invalidity of the pledge agreement, at least until he has paid or tendered to the railway company the full amount of its deposits" (Brief, p. 57).

XI

The Court erred in holding in effect that the receiver could disaffirm the pledge agreement, it having been made in good faith while the bank was solvent and having been executed by the railway company.

XII

The Court erred in its conclusion that "this is not a case" like that "of a solvent bank which has obtained the benefit of a transaction, seeking to avoid, on the

ground of *ultra vires*, returning what it has received" (Opinion, p. 9), because the pledge agreement was made in good faith while the bank was solvent, the railway company deposited its money on the strength of that agreement, and the receiver stands in the shoes of the bank.

XIII

The Court erred in holding in effect that the receiver, as a representative of the bank's creditors, has rights or equities in and to the pledged liberty bonds different from and superior to those of the bank before the receivership (Opinion, p. 8), for the reasons assigned under the foregoing ground of error.

XIV

The Court erred in holding in effect that the case at bar is one "not between the bank and the railway, but between the railway and the bank's creditors" (Opinion, p. 8), for the reasons assigned under the foregoing twelfth ground of error.

XV

The Court erred in holding and in applying to this case its ruling that "It is settled law in the courts of the United States that what a corporation cannot bind itself to do, the courts will not compel (cases); Especially will it not do it in a case of this kind, where the controversy is not between the bank and the railway, but between the

railway and the bank's creditors, the bank having failed, and 'the interest of others than the parties' (case) being involved" (Opinion, p. 8), for the reasons assigned under the foregoing twelfth ground of error, and for the further reason that the facts of this case distinguish it from the citied cases announcing such rule of law.

XVI

The Court erred in overruling and in not sustaining appellant's third specification of error and its point three thereunder reading as follows:

> "The trial court erred in concluding and in holding as a matter of law that the railway company's deposits made subsequent to the pledge of the liberty bonds were general deposits the title to which passed to the bank, and were not special deposits the title to which remained and now is in The Texas and Pacific Railway Company" (Brief, p. 19).
>
> "If the pledge contract is wholly void and of no legal effect, the moneys deposited by the appellant on the faith of that agreement were accepted by the bank as special deposits, the title to which remained and now is in the railway company" (Brief, p. 65).

XVII

Having found that the pledge agreement was invalid, the Court erred in holding in effect that the agreement of deposit in this case definitely fixed the character of

the deposit as general (Opinion, p. 9), because appellant's deposits were made in reliance upon the validity of that agreement.

XVIII

The Court erred in holding that the contract of deposit contained two agreements, viz: "One that the bank should pay back to the railway upon demand the sums deposited with it as other general deposits were. * * * The other is an agreement for security" (Opinion, p. 8), because appellant's deposits were made in reliance upon the validity of that agreement.

XIX

The Court erred in holding "there is no basis at all here for declaring a trust", and in further holding, in effect, that the railway company, being a "general depositor" in the bank, cannot, because its security failed through an invalidity which in law it knew, have the bank converted into a trustee and itself into a *cestui que* trust of the money of the bank to the extent of the amount of its general deposit (Opinion, pp. 9-10), because, if its security was invalid the railway company never became a general depositor and the bank received and held its moneys as special deposits.

XX

The Court erred in overruling and in not sustaining appellant's fourth specification of error and its point four thereunder reading as follows:

> "The trial court erred in concluding and in holding as a matter of law that the railway company is not entitled to recover of and from the bank's receiver a sum equal to the full amount of its deposits, plus interest, as for money had and received" (Brief, p. 19).
>
> "If the pledge contract is wholly void and of no legal effect, the railway company is entitled to recover of and from the receiver a sum equal to the full amount of appellant's deposits, plus interest, as for money had and received" (Brief, p. 69).

XXI

The Court erred in disregarding appellant's alternative plea for money had and received (Tr. 10, Br. 69-73) and in holding that this is not a suit "on the benefits received" but is a suit "upon a contract, to enforce it" (Opinion, p. 9).

XXII

The Court's decision is in conflict with and is contrary to principles and rules of law announced by the Supreme Court in its decisions, among others:

Aldrich v. Chemical National Bank, 176 U. S. 618, 44 L. ed. 611;

Auten v. United States National Bank, 174 U. S. 125, 43 L. ed. 920;

Central Transportation Co. v. Pullman's Palace Car Co., 139 U. S. 24, 35 L. ed. 55;

Citizens National Bank v. Appleton, 216 U. S. 196, 54 L. ed. 443;

Eastern Building and Loan Association v. Williamson, 189 U. S. 122, 47 L. ed. 735;

First National Bank of Charlotte v. National Exchange Bank of Baltimore, 92 U. S. 122, 23 L. ed. 679;

Head v. The University, 86 U. S. 526, 22 L. ed. 160;

Jacksonville, etc., Railway Co. v. Hooper, 160 U. S. 514, 40 L. ed. 515;

Logan County National Bank v. Townsend, 139 U. S. 67, 35 L. ed. 107;

Marine Bank v. Fulton County Bank, 69 U. S. 252, 17 L. ed. 785;

McCullough v. Maryland, 4 Wheaton 216, 4 L. ed. 579;

National Bank v. Matthews, 98 U. S. 621, 25 L. ed. 188;

National Bank v. Whitney, 103 U. S. 99, 26 L. ed. 443;

New York County National Bank v. Massey, 192 U. S. 138, 48 L. ed. 380;

Rankin, Receiver v. Emigh, 218 U. S. 27, 54 L. ed. 915;

Robinson v. Lundrigan, 227 U. S. 173, 57 L. ed. 468;

Scott v. Armstrong, 146 U. S. 499, 36 L. ed. 1059;

Thompson v. St. Nicholas National Bank, 146 U. S. 240, 36 L. ed. 957.

Union Pacific Ry. Co. v. Chicago, etc. Ry. Co., 163 U. S. 564, 41 L. ed. 265;

Wyman v. Wallace, 201 U. S. 230, 50 L. ed. 738.

Appellant has refrained from incorporating any argument in this petition in compliance with the Court's rule XXIX, but respectfully asks leave to file a written argument in support of this petition for rehearing.

Wherefore, premises considered, appellant prays the Court upon a consideration of this petition to set aside its judgment heretofore entered herein, to reverse the decree rendered by the court below, and to remand this

case to that court with instructions to grant the relief for which appellant prays in its amended bill of complaint, and for such other orders and decrees as to this Honorable Court appellant may seem entitled in the premises.

Dated February 28, 1933.

Respectfully submitted,

S. N. RUSSELL,
First National Bank Bldg.,
El Paso, Texas.

DEL W. HARRINGTON,
Bassett Tower,
El Paso, Texas.

T. D. GRESHAM,

M. E. CLINTON,
Texas and Pacific Bldg.,
Dallas, Texas.
Attorneys for Appellant,
The Texas and Pacific Railway Company.

Certificate of Counsel

I, the undersigned, of counsel for appellant, The Texas and Pacific Railway Company, do hereby certify that the foregoing petition for rehearing is presented in good faith and not for delay.

(Signed) M. E. CLINTON,
Of Counsel for Appellant.

IN UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

ORDER DENYING REHEARING—March 8, 1933

It is ordered by the Court that the petition for rehearing filed in this cause be, and the same is hereby, denied.

IN UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

MOTION FOR ORDER STAYING MANDATE—Filed March 18, 1933

To the Honorable, the Judges of the United States Circuit Court of Appeals for the Fifth Circuit:

Comes now The Texas and Pacific Railway Company, appellant, and moves and prays the Court to enter an order herein withholding the mandate and staying the execution and enforcement of its judgment or decree rendered in this cause to enable appellant to perfect an appeal to or apply for and obtain a writ of certiorari from the Supreme Court of the United States, and for grounds of this motion appellant respectfully shows:

I

The Circuit Court of Civil Appeals on January 19, 1933, affirmed the judgment of the trial court in favor of appellee, and this Court on the 8th day of March, 1933, overruled appellant's petition for a rehearing.

II

Appellant will perfect an appeal to or apply for a writ of certiorari from the Supreme Court of the United States within the time allowed by law.

III

The stay order for which appellant prays, if granted, will not subject appellee to any damage because the pledged

liberty bonds are in appellee's possession and by agreement of the parties may be reduced to cash at the option of appellee. And appellant is ready and willing to post such bond as the Court may require under section 350 of title 28 of the United States Code.

Wherefore, appellant prays the Court to grant this application and to enter its order herein withholding the mandate and staying the execution and enforcement of its judgment or decree for a reasonable time to enable appellant to perfect an appeal to or apply for and obtain a writ of certiorari from the Supreme Court of the United States.

Respectfully submitted.

(Signed) S. N. Russell, Del W. Harrington, T. D. Gresham, M. E. Clinton, Attorneys for Appellant.

IN UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

STAY ORDER—Filed March 18, 1933

Upon application of The Texas and Pacific Railway Company, appellant in the above entitled cause, by its counsel, for an order withholding the mandate and staying the execution and enforcement of the judgment or decree of the United States Circuit Court of Appeals for the Fifth Circuit to enable appellant to perfect an appeal to or apply for and obtain a writ of certiorari from the Supreme Court of the United States, and good cause therefor being shown,

It is ordered that the mandate in this cause be and the same hereby is stayed and that the execution and enforcement of said judgment or decree be and it hereby is stayed until appellant, within the time allowed by law, perfects an appeal to the Supreme Court of the United States or applies for a writ of certiorari from that Court, and until the Supreme Court passes upon such application; provided, however, that The Texas and Pacific Railway Company, appellant, give good and sufficient surety, in the sum of One Thousand Dollars, to be approved by a judge of this Court, conditioned that if The Texas and Pacific Railway Company fails to perfect an appeal to or apply for a writ

of certiorari from the Supreme Court of the United States within the time allowed by law, or fails to obtain an order granting its application for any writ of certiorari which it may file, or fails to make its plea good in the Supreme Court, it shall answer for all damages and costs which appellee may sustain by reason of said stay.

Dated this the 17th day of March, 1933.

(Signed) J. C. Hutcheson, Jr., Judge of the United States Circuit Court of Appeals for the Fifth Circuit.

Bond on stay for $1,000.00, approved and filed March 18, 1933, omitted in printing.

Clerk's certificate to foregoing transcript omitted in printing.

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 9, 1933

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fifth Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 37,731. U. S. Circuit Court of Appeals, Fifth Circuit. Term No. 128. The Texas & Pacific Railway Company, petitioner, vs. S. O. Pottorff, receiver of the First National Bank of El Paso, Texas. Petition for a writ of certiorari and exhibit thereto. Filed June 6, 1933. File No. 128, O. T., 1933.

FILE COPY

JUN 6 1933
CHARLES ELMORE CR
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In the
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1933

No. 128

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Petitioner,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT, AND SUPPORTING BRIEF

S. N. RUSSELL,
DEL W. HARRINGTON,
T. D. GRESHAM,
M. E. CLINTON,
Counsel for Petitioner

June 1, 1933.

Warlick Law Printing Co.—Dallas

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In the

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No.....

THE TEXAS AND PACIFIC RAILWAY COMPANY,

Petitioner,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

To the Honorable the Supreme Court of the United States:

Your petitioner, The Texas and Pacific Railway Company, respectfully requests this Court to review by certiorari a judgment of the Circuit Court of Appeals for the Fifth Circuit in which that Court, in affirming a decree of the District Court for the Western District of Texas in favor of respondent has held (1) that a solvent national bank, which has procured the account and deposits of a railroad company by furnishing corporate surety bonds to protect its deposits, has no power to pledge a portion of its assets in lieu of those surety bonds

for the purpose of saving bond premiums and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute company could not be obtained; and (2) that a receiver of the bank, subsequently appointed by the Comptroller of the Currency, may disaffirm such pledge agreement and retain both the pledged assets and the carrier's deposits, although national bank examiners, who learned of the pledge agreement from the books of the bank one month before its failure, made no complaint of the transaction and by their silence permitted the carrier thereafter to make substantial deposits.

Summary Statement of the Matters Involved

Pursuant to an order of the United States District Court for the Western District of Louisiana, Monroe Division, receivers of the Texas and Pacific Railway opened the first account with and made deposits in the First National Bank of El Paso on or about July 10, 1922, and required of the bank a corporate surety bond in the sum of $25,000 to protect their deposits (R. 44-45, 51-52, 88).

Upon the termination of that receivership in May 1924, The Texas and Pacific Railway Company continued its account with and made deposits in the First National Bank of El Paso but required of the bank a

corporate surety bond in the sum of $25,000 to protect its deposits (R. 45, 54, 88). Due to an increase in its deposits, the railway company in April 1927, required the bank to furnish an additional corporate surety bond in the sum of $25,000 (R. 45-46, 55-56, 88). These two bonds, on which the bank paid the premiums, remained in full force and effect until January 30, 1931 (R. 47, 89-90, 92-93) and fully protected at all times your petitioner's deposit balances (R. 45-46, 55-56, 88).

During the month of January 1931, while the First National Bank was solvent and a going concern, its duly authorized active vice president-cashier called upon the president of The Texas and Pacific Railway Company at Dallas, Texas, and in good faith requested him to accept as security for the railway company's deposits a pledge of United States Government Liberty Loan Bonds of the par value of $50,000 in lieu of the two $25,000 surety bonds. In explanation of this request, that bank officer stated that the First National desired to substitute the liberty bonds in order to relieve the bank of the premium payments on the surety bonds (R. 78-79, 89-90). Before making this trip to Dallas, the bank's vice president-cashier knew that the Maryland Casualty Company, surety on one of the $25,000 bonds, intended to "get off all bonds" of the First National Bank; that the bank was "going to have to give up this Maryland Casualty bond"; that the railway company was being asked to accept the liberty bonds in lieu of the surety

bonds partly "because we knew eventually they (Maryland Casualty Company) would ask us to have the bond cancelled, or would not renew it"; and "I did not know when they withdrew we could not get any other surety company, any standard insurance company, to take that risk, but I had a good hunch". But this bank officer admitted that he "did not mention" to the railway company's president "at the time this substitution was made, or at any other time thereafter, this substitution was desired on account of the surety company threatening to cancel its bonds. He never heard of that, so far as I know" (R. 63, 70-72).

The railway president informed the vice president-cashier that it was the policy of the Texas and Pacific to require of depositories adequate security for its deposits, preferably corporate surety bonds; that the railway company would not continue its account with and make deposits in the First National Bank without security; that if the surety bonds were cancelled without the substitution of other adequate security the Texas and Pacific's account would be closed and its deposits withdrawn; but if the bank's officers and attorneys, after an investigation, concluded that the substitution of the liberty bonds in lieu of the surety bonds would be legal and valid in every particular, would constitute and be a binding and enforceable obligation against the bank, and would protect the railway company's deposits as

fully and to the same extent as the surety bonds, the Texas and Pacific would agree to such substitution and to the cancellation of the surety bonds solely for the purpose of enabling the bank to save the bond premiums (R. 79-80, 90-91).

At the request of the carrier's president, the vice president-cashier submitted the proposed substitution plan to the bank's attorneys, and after an investigation they advised the officers of the bank that the substitution could be legally made; that the pledge agreement would be an enforceable obligation against the bank; and that the substituted liberty bonds would protect the railway company's deposits as fully and to the same extent as the surety bonds. At the direction of the bank's officers, its attorneys prepared a pledge agreement which was executed by the First National Bank on January 29, 1931. Thereupon, officers of the bank, pursuant to the pledge agreement and while the bank was solvent and a going concern, deposited with the First National's Trust Officer liberty bonds of the par value of $50,000 as security for the railway company's deposits. All of those liberty bonds were thereafter held by the Trust Officer separate and apart from all assets of the bank, in an envelope bearing the name of The Texas and Pacific Railway Company, and the liberty bonds for which your petitioner sued are the identical bonds which were deposited with such Trust Officer (R. 46-47, 57-59, 91-92).

The officers of the bank concurred in the opinion of its attorneys and so advised the railway company's president. Believing those representations to be true, that rail officer accepted the executed pledge agreement and the liberty bonds which had been placed in the custody of the bank's Trust Officer in lieu of the surety bonds and caused the latter to be cancelled effective January 30, 1931. A full record of this transaction was made on the bank's books on January 29, 1931, and remained on those books continuously thereafter until the receiver took charge of the bank on September 8, 1931. After the liberty bonds had been substituted for the surety bonds, The Texas and Pacific Railway Company, relying upon the pledge agreement and the liberty bonds as security for its deposits, continued its account with and made deposits in the First National Bank and thereafter its average daily deposit balance in that bank substantially equaled $50,000, the total par value of the pledged liberty bonds; and the bank continued to accept and pay the railway company's checks and drafts drawn against its deposits until on or about September 4, 1931, when the bank failed, became insolvent, closed its doors to the public, and refused to accept, honor or pay any other or further checks or drafts drawn by the Texas and Pacific (R. 47, 92-93).

The railway company deposited in the bank during the period January 29, 1931, to August 5, 1931, a total of $132,200.27, and during the period August 6, 1931 to

September 3, 1931, a total of $16,545.48. On the following dates it had on deposit these sums of money:

January 29, 1931	$22,264.10
August 6, 1931	50,428.10
September 3, 1931	54,646.94 (R. 93).

The First National Bank of El Paso over a long period of years has furnished, often at its expense, corporate surety bonds to protect numerous deposits, both public and private, but apparently has not pledged its assets directly to private depositors for that purpose. By substituting the liberty bonds in lieu of the surety bonds as security for the railway company's deposits, the bank saved the premiums on the surety bonds, earned 4-1/4 per cent interest on the liberty bonds and was able to hold the railway company's account and deposits (R. 74, 94).

The Texas and Pacific had $54,646.94 on deposit in the First National Bank on September 4, 1931, which sum of money it was entitled to receive from the bank upon demand. All of these funds, except accrued interest, were deposited by the railway company subsequent to January 29, 1931, the date on which the liberty bonds were substituted in lieu of the surety bonds as security for the Texas and Pacific's deposits, and all of those funds were collected by the railway company for common carrier services rendered in the transportation of both interstate and intrastate commerce (R. 48, 93).

The Comptroller of the Currency on or about September 6, 1931, duly and regularly appointed respondent S. O. Pottorff receiver of The First National Bank of El Paso, and on or about September 8, 1931 he took charge of the bank's affairs, assets and securities and its Trust Department in which the pledged liberty bonds were held as security for the railway company's deposits (R. 48, 88)[1].

National bank examiners acting under the supervision and control of the Comptroller of the Currency made an examination of the First National Bank commencing at 8 o'clock a. m. on August 6, 1931, and ending at noon on August 20, 1931, and their report to the Comptroller, covering the condition of the bank, forwarded after the bank closed, showed that liberty bonds of the par value of $50,000 were then pledged to secure the railway company's deposits. They obtained this information from the books of the bank probably during the first two or three days after the examination. The officers of the bank were never notified or advised by either the bank examiners or the Comptroller of the Currency that the pledge of liberty bonds to secure the railway company's account was either irregular, beyond the powers of the bank, or illegal, and no complaint of any character concerning

[1]The receiver, pursuant to an agreement between the parties dated August 12, 1932, sold the liberty bonds for $52,273, which sum of money is being held by it "separate and apart from all assets" of the First National Bank of El Paso "expressly subject to and for the purpose of satisfying any and all liens, claims or judgments which the courts may adjudicate that The Texas and Pacific Railway Company has, or to which it may be entitled, in and to said liberty bonds, or the proceeds from the sale or sales thereof".

the substitution agreement and the pledge of the liberty bonds was ever made to the bank's officers, or any of them, by the bank examiners or the Comptroller of the Currency (R. 94-95).

When the examination of the First National Bank began on August 6, 1931, the railway company had $50,-428.10 on deposit, and between that date and September 3, 1931, the Texas and Pacific deposited an additional $16,545.48, relying upon the liberty bonds and the pledge agreement as security (R. 93-94).

The Texas and Pacific Railway Company demanded of the receiver that he pay to it the sum of $54,646.94, which the receiver refused to do; the railway company then demanded that the receiver deliver to it the pledged liberty bonds and credit the company's claim with the market value of those bonds at the time of delivery, but this the receiver refused to do; and the railway company then demanded that the receiver sell the pledged liberty bonds and apply the proceeds of the sale to the liquidation of the company's claim, but the receiver refused to comply with this demand (R. 48-49, 88).

Thereupon, The Texas and Pacific Railway Company by its bill of complaint filed March 1, 1932, amended May 25, 1932, brought this action in the United States District Court for the Western District of Texas, El Paso Division, against S. O. Pottorff, Receiver of The First National Bank of El Paso (1) to recover of and from the receiver the liberty bonds pledged by the bank

in good faith while solvent to secure the railway company's deposits, or (2) to compel the receiver to sell those liberty bonds and deliver the proceeds of such sale to the railway company in partial settlement of its claim of $54,646.94 against the bank and its receiver; or, in the alternative, (3) to compel the receiver to return to the railway company its deposits in the First National Bank as of September 4, 1931, or (4) to recover of and from the receiver, as for money had and received, a sum of money equal to the railway company's deposits in the bank on that date (R. 1-20).

The receiver moved to dismiss the amended bill for want of equity and subsequent to that motion filed an answer alleging the invalidity of the pledge agreement. In addition, the receiver filed a cross-bill against the railway company seeking a judgment declaring the pledge agreement null and void, establishing the receiver's title to the liberty bonds and enjoining the railway company from asserting any rights thereto. To this cross-bill the Texas and Pacific filed a motion to dismiss for want of equity (R. 20, 21-27, 27-30, 31).

The trial court heard the case upon its merits and after argument overruled both motions to dismiss and rendered a decree on the cross-bill in favor of the receiver. From that decree the railway company prosecuted an appeal to the Circuit Court of Appeals for the Fifth Circuit, which Court on January 19, 1933, affirmed the decree of the trial court (R. 126) and on March 8,

1933, overruled the railway company's petition for a rehearing (R. 143).

Reasons Relied Upon for an Allowance of the Writ

Your petitioner respectfully represents that this Court should review by certiorari the judgment in this case by the Circuit Court of Appeals for the Fifth Circuit for the following reasons:

1. The Circuit Court has decided important questions of federal law which have not been, but should be, settled by the Supreme Court. Those questions are:

(a) Did Congress in authorizing a national bank "to exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; * * * by receiving deposits; * * *"[1] empower those banks while solvent to pledge in good faith a portion of their assets as security for deposits which they desire to procure or to retain?

(b) Is a pledge by a solvent national bank of a portion of its assets made in good faith as security for deposits ultra vires the bank when that pledge is made in lieu of corporate surety bonds theretofore furnished by the bank, at its expense, to procure such deposits, and for the purpose of saving bond premiums and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute company could not be obtained?

---

[1]Act of June 3, 1864, c. 106; U. S. C. A. Title 12, chap. 2, sec. 24.

(c) When a solvent national bank, in order to procure deposits, at its expense furnishes a depositor with corporate surety bonds as security and thereafter induces such depositor to accept a pledge of a portion of the bank's assets in lieu of those surety bonds, may the receiver of that bank, subsequently appointed by the Comptroller of the Currency, repudiate the pledge agreement and retain both the pledged assets and the deposits after national bank examiners, before the bank's failure, learned of the pledge agreement from an examination of the bank's books but made no complaint of the transaction?

(d) Do deposits made in a national bank in reliance upon the security of the bank's pledged assets, which the bank while solvent has induced the depositor to accept in lieu of surety bonds, become general deposits and assets of the bank or does the bank and its subsequently appointed receiver hold those funds as special deposits in trust for the use and benefit of the depositor?

2. The Circuit Court of Appeals has decided federal questions in a way probably in conflict with applicable decisions of the Supreme Court.

In rejecting the railway company's contention that the pledge agreement was valid because its deposits were loans to the bank and a national bank may pledge its assets to secure a loan, the Circuit Court, following the opinion of the Supreme Court of the State of Arkansas in *McCown v. Edwards, 48 S. W. (2d) 558*, held that "a deposit is one thing, a loan another" (R. 124). It appears

that this holding is in conflict with two decisions of the Supreme Court in which it was held that "the deposit of money by a customer with his banker is one of loan, with the superadded obligation that the money is to be paid when demanded, by a check";[1] and that "all deposits made with bankers may be divided into two classes, namely: those in which the bank becomes bailee of the depositor, the title to the thing deposited remaining with the latter; and that other kind of deposit of money peculiar to banking business, in which the depositor, for his own convenience, parts with the title to his money and loans it to the banker; and the latter, in consideration of the loan of the money and the right to use it for his own profit, agrees to refund the same amount, or any part thereof, on demand".[2] And it is here noted that the Supreme Court also has held that a national bank may secure a loan, although the power "is not expressly given by the (national bank) act", because a bank has the implied power "to incur liabilities in the regular course of its business",[3] and because "it is not in terms prohibited by the National Bank Act".[4] The foregoing quotations were set out on pages 26-28 of your petitioner's brief in the Circuit Court, and those cases were again called to that Court's attention on pages 11

[1]New York County National Bank v. Massey, 192 U. S. at page 145, 48 L. ed. p. 383.

[2]Marine Bank v. Fulton County Bank, 69 U. S. at page 256, 17 L. ed. p. 787.

[3]Aldrich v. Chemical National Bank, 176 U. S. at page 626, 44 L. ed. p. 614.

[4]Wyman v. Wallace, 201 U. S. at page 243, 50 L. ed. 742.

and 12 of the railway company's petition for rehearing (R. 139, 140).

It does not appear that the Circuit Court, in concluding that the pledge agreement was ultra vires, was guided by these rules of construction laid down by the Supreme Court:

> "* * * Whatever may fairly be regarded as incidental to, or consequential upon those things which the Legislature has authorized, ought not, unless expressly prohibited, to be held, by judicial construction, to be ultra vires". *Jacksonville, Mayport, Pablo R. & Nav. Co. v. Hooper, 160 U. S. 514, 523, 40 L. ed. p. 523.*
>
> "* * * When a contract is not on its face necessarily beyond the scope of the power of the corporation by which it was made, it will, in the absence of proof to the contrary, be presumed to be valid. Corporations are presumed to contract within their powers. The doctrine of ultra vires, when invoked for or against a corporation, should not be allowed to prevail where it would defeat the ends of justice or work a legal wrong. * * *". *Ohio & M. R. Co. v. McCarthy, 96 U. S. at page 258, 24 L. ed. p. 695.*

It is clear that the Circuit Court erroneously put the strictest possible construction upon the phrase "as shall be necessary to carry on the business of banking", in section 24 of the National Bank Act, and held in effect that the word "necessary" was used as a synonym for the word "indispensable", contrary to the definition of that term given by the Supreme Court in *McCullough v.*

Maryland, 4 Wheaton 316, 4 L. ed. 579. In that case Chief Justice Marshall, in affirming the incidental power of the Federal Government to incorporate a national bank, stated:

> "To its (the constitution's) enumeration of powers is added that of making 'all laws which shall be *necessary* and proper, for carrying into execution the foregoing powers, and all other powers vested by this constitution, in the Government of the United States, or in any department thereof'. (Wheat. pp. 412-13, L. ed. pp. 602-603).
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> * * * * *
>
> "The argument on which most reliance is placed, is drawn from the peculiar language of this clause. Congress is not empowered by it to make all laws, which may have relation to the powers conferred on the government, but such only as may be '*necessary* and proper' for carrying them into execution. The word '*necessary*' is considered as controlling the whole sentence, and as limiting the right to pass laws for the execution of the granted powers, to such as are indispensable, and without which the power would be nugatory. That it excludes the choice of means, and leaves to Congress, in each case, that only which is most direct and simple.
>
> "Is it true that this is the sense in which the word 'necessary' is always used? Does it always import an absolute physical necessity, so strong that one thing, to which another may be termed necessary, cannot exist without that other? We think it does not. If reference be had to its use, in the common affairs of the world, or in approved authors, we find that it frequently imports no more than that one thing is *convenient*, or *useful*, or essential to another. To employ the means necessary to an end,

> is generally understood as employing any means calculated to produce the end, and not as being confined to those single means, without which the end would be entirely unattainable. Such is the character of human language, that no word conveys to the mind, in all situations, one single definite idea; and nothing is more common than to use words in a figurative sense. Almost all compositions contain words, which, taken in their rigorous sense, would convey a meaning different from that which is obviously intended. It is essential to just construction, that many words which import something excessive should be understood in a more mitigated sense—in that sense which common usage justifies. The word *'necessary'* is of this description" (our italics) (Wheat. pp. 413-414, L. ed. p. 603).

It appears that the decision of the Circuit Court of Appeals conflicts with the views of the Supreme Court because, as stated by it in *First National Bank of Charlotte v. National Exchange Bank of Baltimore, 92 U. S. at page 127, 23 L. ed. 671*, national banks may do "whatever natural persons could do under like circumstances", but "subject to law", as provided in the Act, which term this Honorable Court in *Head v. The University, 86 U. S. at page 530, 22 L. ed. 160*, defined to mean "subject to whatever law" the legislative body "might think fit to pass"; and Congress has not prohibited a pledge of this character by a solvent national bank. Also, the opinion of the Circuit Court appears to be in conflict with the decision of the Supreme Court in *Scott v. Armstrong, 146*

U. S. at page 510, 36 L. ed. 1063, in which the Court, construing section 52 of the National Bank Act,[1] stated:

> "Undoubtedly any disposition by a National Bank, being insolvent or in contemplation of insolvency, of its choses in action, securities or other assets, made to prevent their application to the payment of its circulating notes, or to prefer one creditor to another, is forbidden; but liens, equities, or rights arising by express agreement, or implied from the nature of the dealings between the parties, or by operation of law, prior to insolvency and not in contemplation thereof, are not invalidated. The provisions of the Act are not directed against all liens, securities, *pledges* or equities, whereby one creditor may obtain a greater payment than another, but against those arising or in contemplation of insolvency".

The four preceding quotations were set forth on pages 38-40, 22 and 25, respectively, of the railway company's brief in the Circuit Court, and reference was made to those cases in its petition for rehearing (R. 139, 140).

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[1]Section 52 of the National Bank Act of 1864 (12 U. S. C. A. sec. 91) reads in part:

> "All transfers of the notes, bonds, bills of exchange, or other evidences of debt owing to any national banking association, or of deposits to its credit; all assignments of mortgages, sureties on real estate, or of judgments or decrees in its favor; all deposits of money, bullion, or other valuable thing for its use, or for the use of any of its shareholders or creditors; and all payments of money to either, **made after the commission of an act of insolvency, or in contemplation thereof, made with a view to prevent the application of its assets in the manner prescribed by this chapter, or with a view to the preference of one creditor to another,** except in payment of its circulating notes, shall be utterly null and void * * *" (emphasis supplied).

In disposing of the railway company's plea of estoppel, the Circuit Court misapplied principles of law announced by the Supreme Court in these three cases: *California Nat. Bank v. Kennedy, 167 U. S. 362; Union Pac. Ry. v. Chicago, 163 U. S. 564;* and *Central Transportation Co. v. Pullman Car Co., 139 U. S. 60;* and it was induced so to do by an erroneous belief that the receiver was entitled to some unusual protection because "the controversy is not between the bank and the railway, but between the railway and the bank's creditors, the bank having failed, and 'the interest of others than the parties' * * * being involved" (R. 125). In reaching this conclusion, the Circuit Court apparently gave no consideration to the decision of the Supreme Court in *Scott v. Armstrong, 146 U. S. at page 507, 36 L. ed. p. 1062,* in which this Court stated that a receiver of a national bank takes its assets, in the absence of a statute to the contrary, "subject to all claims and defenses that might have been interposed as against the insolvent corporation before the liens of the United States and of the general creditors attached". It also appears that the Circuit Court put out of mind those cases of the Supreme Court holding that "corporations as much as individuals are bound to good faith and fair dealing, and the rule is well settled that they cannot, by their acts, representations or silence, involve others in onerous engagements and then turn round and disavow their acts and

defeat the just expectations which their own conduct has superinduced".[1]

The Circuit Court has sanctioned the repudiation by a receiver of an agreement which it, while solvent, has induced a depositor to make for the benefit of the bank. This action of the lower court probably is in conflict with those decisions of the Supreme Court in which it has been held that no one but the sovereign is permitted to assert that a corporation's contract is ultra vires,[2] unless by statute they are authorized so to do.[3] The decision of the Circuit Court was based upon the assumption that the receiver had some peculiar property rights, exceeding those of the bank while solvent, in and to the pledged liberty bonds and the deposits which they secured (R. 125), but this assumption appears to be in conflict with the statement of the Supreme Court in *Scott v. Armstrong, 146 U. S. at page 507, 36 L. ed. 1062*, to the effect that a receiver of a national bank takes the assets and moneys passing into his possession "as a mere trustee for creditors, and not for value and without notice and, in the absence of statute to the contrary, subject to all claims and defenses that might have been interposed as against the insolvent corporation before

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[1]Chicago, R. I. & P. Co. v. Howard, 74 U. S. at page 392, 19 L. ed. p. 121.

Zabriskie v. Cleveland, C. & C. R. Co., 64 U. S. at page 381, 16 L. ed. p. 498.

[2]Jones v. New York Guaranty & I. Co., 101 U. S. at page 622, 25 L. ed. p. 1035.

Sioux City Terminal R. & Wareh. Co. v. Trust Co. of N. A., 173 U. S. at page 110, 43 L. ed. p. 632.

[3]Blair v. Chicago, 201 U. S. page 451, 50 L. ed. 822.

the liens of the United States and of the general creditors attached".

3. The Circuit Court of Appeals has decided important questions of general law in a way probably untenable or in conflict with the weight of authority.

Your petitioner contended in the lower courts that if the pledge agreement was in fact ultra vires, the bank and its receiver hold the railway company's deposits not as general assets of the bank but as a trust fund to which petitioner is entitled, and that the return of its deposits, or their equivalent, would not constitute an unlawful preference under the National Bank Act. The Circuit Court conceded that prior to the pledge agreement the railway company's deposits "were fully protected and their repayment guaranteed by corporate surety bonds" and that "on January 29, 1931, the bank being still a solvent, going concern, the railway was induced by the bank to permit it to substitute for the surety bonds theretofore securing the deposits the Liberty Loan bonds in question", but the Court erroneously concluded there were two agreements between the railway company and the bank,—

> "One, that the bank should pay back to the railway upon demand the sums deposited with it as other general deposits were. This entirely valid contract the receiver has recognized, and has offered to pay the Railway a dividend on account of it. The other is an agreement for security. This we have found to be invalid and without contractual force as beyond the corporate powers" (R. 125).

Having reached this conclusion, the Circuit Court further held:

> "Here is a contract for depositing, which was valid, and one for security which was invalid because of want of power in the bank, of which want of power appellant was as fully charged with knowledge as the bank was.
>
> "The result is simply that though the railway has the right to press its claim for its debt, it cannot do so for the security" (R. 126).

The holding of the Circuit Court that there were two separate and distinct contracts, one of deposit and the other for security, is contrary to the trial court's findings of fact, approved by the attorney for the receiver (R. 95), that the president of the railway company informed the vice president-cashier "that under no circumstances would The Texas and Pacific Railway Company continue its account with and deposits in the First National Bank of El Paso without full and adequate security" (R. 90); and that the railway company's president, believing as true the representations of the bank's officers and attorneys that the pledge agreement and liberty bonds "would protect the deposits of The Texas and Pacific Railway Company in The First National Bank of El Paso as fully and to the same extent as said corporate surety bonds", accepted the pledge agreement and those bonds, cancelled the surety bonds and thereafter continued its account with and made deposits in the First National Bank "relying upon said pledge agree-

ment and liberty bonds as security for its deposits" (R. 92-93).

Furthermore, if it be true, as held by the Circuit Court, that the pledge agreement was ultra vires and that the railway company was charged with this knowledge as fully as the bank itself, those facts alone would not convert your petitioner's deposits into general assets of the bank under the circumstances of this case. The agreement of deposit and not the legal knowledge of the depositor determines the character of the deposit, and the deposit agreement in this case in legal effect was that the railway company agreed that its deposits might become the property of the bank if they were secured; otherwise not.

However, your petitioner questions the correctness of the Circuit Court's holding. Whether or not the bank had the power to make the pledge is at most a mixed question of law and fact, since the bank is expressly authorized to exercise all such incidental powers as shall be necessary—that is, convenient or useful[1]—to carry on the business of the bank, and what may be convenient or useful to it is purely a fact question peculiarly within the knowledge of the bank's officers. They represented and the record shows that the pledge agreement was convenient and useful to the bank; these facts the receiver has not disproved.

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[1]McCullough v. Maryland, supra.

There is some intimation in the Circuit Court's opinion (R. 125), although no positive statement, that a recovery by the railway company of the full amount of its deposits or their equivalent would constitute an unlawful preference over other creditors, but such is not the case. The receiver of a national bank is directed by section 192 of the Act to take charge of all the bank's "assets" and to pay over to the Treasurer of the United States, subject to the order of the Comptroller, all moneys received from the collection of debts, claims, and the sale of property. And the Comptroller by section 194 is directed to make a "ratable dividend" from time to time, under certain conditions, of the moneys turned over to him by the receiver; but the Supreme Court has held in *Scott v. Armstrong, 146 U. S. at page 510, 36 L. ed. p. 1063*, that "the requirement as to ratable dividends, is to make them from what belongs to the bank, and that which at the time of the insolvency belongs of right to the debtor does not belong to the bank". It seems, therefore, that this statement of the Supreme Court, as applied to the facts of this case, is in conflict with the holding of the Circuit Court that the moneys of the railway company were general deposits and became assets of the bank to be distributed by the receiver ratably among all creditors.

The Circuit Court held that the record does not "support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is

a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" (R. 124). In thus holding, in effect, that the railway company had the burden of proving that it is the practice and custom of national banks to make such pledge agreements, and that the making of them is indispensable to the banking business, it appears that the Circuit Court's decision is in conflict with the principles of law announced by the Supreme Court to the effect that corporations are presumed to contract within their powers, and, *in absence of proof to the contrary*, their contracts are presumed to be valid when not foreign to the purposes for which the corporation is created.[1] The receiver did not rebut this presumption; in fact, he offered no testimony at the trial of the case. If the railway company had any burden of proof it was merely to show that the pledge agreement, in the language of the Supreme Court, was "convenient or useful"[2] to the bank. This burden was fully met when your petitioner proved, as found by the trial court, that the First National Bank by substituting the liberty bonds in lieu of the surety bonds "saved the premiums on said surety bonds, earned 4-1/4% interest on said liberty bonds, and was able to hold the railway company's account" (R. 94).

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[1]Ohio & M. R. Co. v. McCarthy, 96 U. S. at page 258, 24 L. ed. p. 695.
Union Pac, R. Co. v. Chcago, R. I. & P. R. Co., 163 U. S. 564, 41 L. ed. 265.
[2]McCullough v. Maryland, supra.

As an alternative plea the railway company alleged that if the pledge agreement was unenforceable it was entitled to recover from the receiver, as for money had and received, the full amount of its deposits in the bank on September 4, 1931, the date of its failure (R. 10); and a prayer for this alternative relief was included in its amended bill (R. 12). The Circuit Court disposed of this contention in the following language:

> "This is not a case like Aldrich v. Chemical Nat. Bank, 176 U. S. 636; Citizens Nat. Bank vs. Appleton, 216 U. S. 206; Schneider v. Thompson, 58 Fed. (2) 98, of a solvent bank which has obtained the benefit of a transaction, seeking to avoid, on the ground of ultra vires, returning what it has received. In those cases the suit was not on the contract, but on the benefit received. This is not such a case. It is upon a contract, to enforce it" (R. 125).

Your petitioner believes that this disposition by the Circuit Court of its plea for money had and received is in conflict with principles of law announced by the Supreme Court in a number of cases, including *Central Transportation Co. v. Pullman Car Co., 139 U. S. at page 60, 35 L. ed. p. 69; Aldrich v. Chemical National Bank, 176 U. S. at page 636, 44 L. ed. p. 618; Citizens' National Bank v. Appleton, 216 U. S. at page 206, 54 L. ed. p. 446.*

4. In deciding the case at bar, the Circuit Court of Appeals for the Fifth Circuit based its decision upon principles of law in conflict with those announced by other Circuit Courts of Appeal.

The Circuit Court of Appeals for the Eighth Circuit in *American Nat. Bank v. National Wallpaper Co., 77 Fed. 85,* in considering the power of a national bank to buy and sell goods and its liability for their purchase price, held:

> "'The great mass of judicial authority', says Judge Thompson, 'seems to be to the effect that, where a private corporation has entered into a contract in excess of its granted powers, and has received the fruits or benefits of the contract, and an action is brought against it to enforce the obligation on its part, it is estopped from setting up the defense that it had no power to make it' Thomp. Corp. sec. 6016. Continuing the subject, the learned author further says it is a general principle of law that no party will be permitted to set up the defense of ultra vires while retaining the fruits or the benefits of the contract. This doctrine rests upon the unanswerable ground thus stated in Pennsylvania by Mr. Justice Porter: 'A man who has enjoyed a privilege has no right to say that because he ought not to have enjoyed it he will not pay for it. However unlawful the act, it would be unsound policy to give him this immunity.' Id. sec. 6015. The reason of the rule is that honesty and fair dealing are the highest public policy, and that a private corporation, which is a mere collection of individuals, is no more privileged to repudiate its engagements, and act dishonestly, than a single individual is. Id. sec. 6017. Where, therefore, a corporation purchases property contrary to a prohibition, or without an authorization in its charter, it cannot retain the property, and refuse to pay the price, or set up the defense of ultra vires when sued for the same. Id. sec. 6018. The authorities supporting the text of the learned author are too numerous to require

citation. The doctrine has become familiar learning" (pp. 93-94).

Williams v. American Nat. Bank, 85 Fed. 376, also decided by the Circuit Court of Appeals for the Eighth Circuit, was a case in which the plaintiff brought an action against the bank and its receiver to recover $28,250 alleged to be due the plaintiff upon a verbal contract pursuant to which the plaintiff loaned the bank that sum of money to be repaid upon thirty days' notice. On December 8, 1890 the plaintiff demanded payment which was refused; on the next day the bank became insolvent and the Comptroller of the Currency placed it in the hands of a receiver. Upon plaintiff's demand the receiver refused to pay her the money. The defendants contended that the transaction was a purchase of the bank's stock, and that a certificate was delivered to Williams. In her reply, plaintiff alleged that the stock was taken as collateral security for her money. "About the 1st of January, 1890, *the cashier of the bank, knowing its embarrassed condition, to induce her to let her money remain with the bank, persuaded her to believe that a certificate of stock in the bank would be a better security for the money than a certificate of deposit*" * * * (our italics). In reversing a judgment in favor of the defendants, the Circuit Court held:

> "The plea of ultra vires interposed against the contract declared on is not tenable. The plaintiff's action, in its essence, is not predicated upon, nor

> is it for the enforcement of, a contract for stock. In effect, the action is for money had and received. It is to recover the amount of money deposited and loaned by the plaintiff with and to the bank. The bank owes the plaintiff for the money left by her with it, independent of the certificate of stock. Such certificate, according to her contention, having been issued by the bank merely as collateral security for the money received from the plaintiff, it is a matter of entire indifference whether that certificate of stock be with or without value, or invalid in law for the want of power on the part of the bank or authority of the cashier to issue it as collateral security for a loan of money made to it. The plaintiff in the petition tenders back to the bank the certificate of stock, and demands her money. It is no defense to an action for money had and received, based upon a good consideration, both in law and morals, for the bank to say that the collateral security it put up with the plaintiff was issued without authority. This proposition so stands to reason and justice as not to require any authorities for its support" (p. 379).

Burrowes v. Nimocks, 35 Fed. (2d) 152, by the Fourth Circuit Court of Appeals, was a case in which the receiver of the First National Bank of Fayetteville, N. C., contended that the bank's vice president had no authority to secure deposits of Cumberland County by a pledge and transfer of certain notes to the treasurer of the county. In dealing with the receiver's contention that the bank's officer had no authority to secure the deposit, which the court found to be in the nature of a call loan, and which the laws of North Carolina required to be secured, Judge Parker stated:

> "The vice president was expressly authorized to seek it; and this authority carried by *necessary implication* the power to give the security necessary to obtain it" (our italics) (p. 154).

Also, the Fourth Circuit Court of Appeals in *Schumaker v. Eastern Bank & Trust Co., 52 Fed. (2d) 925*, by Judge Parker, stated:

> "Whether a bank may pledge its assets for the security of an ordinary depositor is a question as to which there is conflict of authority. * * * Although some of the cases draw a distinction between a pledge of assets to secure a deposit of public funds and a pledge to secure a private deposit, there would seem to be, in the absence of statute, no valid basis for such distinction; * * *".

It may be that the foregoing statement of Judge Parker in the Schumaker case can be classed as obiter dictum, but it clearly indicates that should questions such as those in the case at bar be submitted to the Fourth Circuit Court of Appeals, that Court would render a decision contrary to that handed down in this case by the Circuit Court for the Fifth Circuit.

Prayer for Writ

WHEREFORE, your petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Honorable Circuit Court of Appeals for the Fifth Circuit, commanding that Court

to certify and send to the Supreme Court a full and complete transcript of the record and all of the proceedings in the case numbered and entitled on its docket, "No. 6748, The Texas and Pacific Railway Company, Appellant, v. S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, Appellee", to the end that this cause may be reviewed and determined by this Honorable Court as provided by the statutes of the United States; and that the judgment of the Circuit Court of Appeals for the Fifth Circuit be reversed by this Honorable Court, and for such further relief as the Court may deem proper.

Dated at Dallas, Texas, June 1, 1933.

Respectfully submitted,

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Petitioner.

By T. D. Gresham
Of Counsel.

In the
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1933

No.....

THE TEXAS AND PACIFIC RAILWAY COMPANY

Petitioner,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,

Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Opinion in the Court Below

The opinion of the Circuit Court of Appeals for the Fifth Circuit in this case, styled *Texas & P. Ry. Co. v. Pottorff*, is reported on pages 1-5 of Vol. 63 of the Federal Reports (Advance Sheet No. 1).

Jurisdiction

(a) The judgment to be reviewed is dated January 19, 1933 (R. 119, 126), and the railway company's petition for rehearing was denied on March 8, 1933 (R. 143). By order dated March 17, 1933, the Circuit Court stayed

the mandate until the Supreme Court acts upon this petition for a writ of certiorari (R. 144-145).

(b) The statutory provision which is believed to sustain the jurisdiction of this Honorable Court is section 347 of Title 28, United States Code (Judicial Code, section 240, amended).

(c) This case involves a construction of the National Bank Act of June 3, 1864, and particularly that portion of the Act enumerating the powers of national banks (section 24, Title 12, United States Code). Specifically, the Court is called upon to determine, among other things, whether or not (1) a solvent national bank which has procured the account and deposits of a railroad company by furnishing corporate surety bonds to protect its deposits, has the power to pledge a portion of its assets in lieu of those surety bonds for the purpose of saving bond premiums and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute company could not be obtained; and (2) whether a receiver of that bank subsequently appointed by the Comptroller of the Currency may disaffirm such pledge agreement and retain both the pledged assets and the carrier's deposits, although national bank examiners who learned of the pledge agreement from the books of the bank one month before its failure made no complaint of the transaction, and by their silence permitted the carrier thereafter to make substantial deposits (R. 43-49, 88-95). The Circuit Court answered

the first question negatively and the second question affirmatively (R. 124-126), contrary, as petitioner believes, to applicable decisions of this Honorable Court, and in a way probably untenable or in conflict with the weight of authority. These specific questions have not been, but should be, settled by the Supreme Court.

(d) It is believed these cases sustain the Supreme Court's jurisdiction:

First National Bank v. Chicago T. & T. Co., 198 U. S. 280, 49 L. ed. 1051.

Texas & N. O. R. Co. v. Brotherhood Ry. & S. S. Clerks, 281 U. S. 548, 74 L. ed. 1034.

Statement of the Case

The statement of the case in the preceding petition, pages 2-11, is hereby adopted and made a part of this brief.

Specification of Errors

In affirming the judgment of the trial court in favor of respondent, the Circuit Court of Appeals for the Fifth Circuit erred in the following particulars:

(1) The Court erred in its finding that the record is "devoid of affirmative proof that the thing the bank did * * * is at all a necessary or desirable practice" (R. 121).

(2) The Court erred in concluding that the record does not "support the finding necessary to be made if

the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" (R. 124).

(3) The Court erred in its finding and conclusion that the record "shows that with the same uniformity which has attended the recognition of the power of national banks to secure public deposits by pledge, the Comptroller has ruled that they may not do so in the case of private deposits" (R. 121).

(4) The Court erred in holding that "the judicial knowledge of banking practices and customs which we may take establishes" that the giving of pledges for private deposits is not a reasonable incident to the business of receiving deposits and is not necessary to the proper conduct of the business of a national bank; and the Court further erred in basing its decision adverse to petitioner in part upon such judicial knowledge (R. 124).

(5) The Court erred in holding that "a deposit is one thing, a loan another", and in rejecting "the view that implied authority to pledge assets as security for loans extends to pledging them to secure deposits" (R. 124).

(6) The Court erred in holding that "generally speaking a bank's general powers do not authorize it to pledge assets for deposits", that the contract for security "was invalid because of want of power in the bank", that "this bank had no such power * * * because no ex-

press power to do so has been conferred upon it by statute", and because the record does not "support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" (R. 124).

(7) The Court erred in holding in effect that to sustain the bank's implied power to make the pledge agreement, petitioner had the burden of affirmatively proving that such agreement was "necessary to the proper conduct of the business of a national bank" and "accords with national banking practices and customs" (R. 121, 124).

(8) The Court erred in holding that petitioner "was as fully charged with knowledge as the bank was" of the latter's "want of power" to make the contract for security (R. 126).

(9) The Court erred in holding in effect that the receiver could disaffirm the pledge agreement (R. 125).

(10) The Court erred in its conclusion that "this is not a case" like that "of a solvent bank which has obtained the benefit of a transaction, seeking to avoid, on the ground of ultra vires, returning what it has received" (R. 125).

(11) The Court erred in holding in effect that the receiver, as a representative of the bank's creditors, has

rights or equities in and to the pledged liberty bonds different from and superior to those of the bank before the receivership (R. 125).

(12) The Court erred in holding in effect that the case at bar is one "not between the bank and the railway, but between the railway and the bank's creditors" (R. 125).

(13) The Court erred in holding in effect that the receiver was not estopped to assert the invalidity of the pledge agreement (R. 125).

(14) The Court erred in holding in effect that the agreement of deposit in this case definitely fixed the character of the deposit as general (R. 126).

(15) The Court erred in holding that the contract of deposit contained two agreements, viz.: "One, that the bank should pay back to the railway upon demand the sums deposited with it as other general deposits were. * * * The other is an agreement for security" (R. 125).

(16) The Court erred in holding "There is no basis at all here for declaring a trust", and in further holding, in effect, that the railway company, being a "general depositor" in the bank, cannot, because its security failed through an invalidity which in law it knew, have the bank converted into a trustee and itself into a *cestui que* trust of the money of the bank to the extent of the amount of its general deposit (R. 126).

(17) The Court erred in disregarding petitioner's alternative plea for money had and received and in holding that this is not a suit "on the benefits received" but is a suit "upon a contract, to enforce it" (R. 125).

(18) The Court erred in concluding and in holding as a matter of law that the bank's pledge of liberty bonds to secure the railway company's deposit was ultra vires and void.

(19) The Court erred in concluding and in holding as a matter of law that the receiver is not estopped from asserting the invalidity of the pledge agreement without returning or tendering back to the railway company the full amount of its deposits.

(20) The Court erred in concluding and in holding as a matter of law that the railway company's deposits made subsequent to the pledge of the liberty bonds were general deposits, the title to which passed to the bank and were not special deposits the title to which remained and now is in The Texas and Pacific Railway Company.

(21) The Court erred in concluding and in holding as a matter of law that the railway company is not entitled to recover of and from the bank's receiver a sum equal to the full amount of its deposit as for money had and received.

(22) The Court erred in holding in effect as a matter of law that a payment by the receiver to The Texas and Pacific Railway Company of the full amount of its

deposit would be an unlawful preference and prohibited by the National Bank Act.

Argument

For the sake of brevity, and in order to avoid duplication, your petitioner by reference will incorporate as a part of this argument certain of the reasons assigned in its petition for an allowance of a writ of certiorari in this case.[1] This argument, therefore, will be limited to a statement of points and authorities, appropriate references to the foregoing petition, and such supplemental argument as to your petitioner may appear helpful.

1. A solvent national bank has the power to pledge, as security for a deposit which it desires to procure and/or retain, a portion of its assets equivalent to that deposit.

New York County National Bank v. Massey, 192 U. S. 138, 145, 48 L. ed. 380, 383; Marine Bank v. Fulton County Bank, 69 U. S. 252, 17 L. ed. 785, 787; Auten v. United States National Bank of New York, 174 U. S. 125, 43 L. ed. 920, 926; Aldrich v. Chemical National Bank, 176 U. S. 618, 626, 44 L. ed. 611, 614; Wyman v. Wallace, 201 U. S. 230, 243, 50 L. ed. 738, 742; Jacksonville, Mayport, Pablo R. & Nav. Co. v. Hooper, 160 U. S. 514, 525, 40 L. ed. 515, 523; Ohio & M. R. Co. v. McCarthy, 96 U. S. 258, 24 L. ed. 693, 695-696; Union Pacific R. Co. v. Chicago, R. I. & P. R. Co., 163 U. S. 564,

[1]Petition for writ of certiorari, pp. 11-29, supra.

581, 41 L. ed. 265, 271; Pittsburgh, C. & St. L. R. Co. v. Keokuk & H. Bridge Co., 131 U. S. 371, 384-385, 33 L. ed. 157, 161-162; McCullough v. Maryland, 4 Wheaton 316, 412-414, 4 L. ed. 579, 603; First National Bank of Charlotte v. National Exchange Bank of Baltimore, 92 U. S. 122, 23 L. ed. 679, 681; Head v. The University, 86 U. S. 526, 22 L. ed. 160; Scott v. Armstrong, 146 U. S. 499, 510, 36 L. ed. 1059, 1063.

Your petitioner adopts as its argument under this point the statements containe don pages 12 to 20 of the foregoing petition, being the second division of the reasons relied upon for an allowance of a writ of certiorari in this case.

It is noted that the Supreme Court has cited with approval quotations from Morse on Banks and Banking[1] and your petitioner respectfully calls the Court's attention to this statement by that eminent text writer:

> "A bank may secure persons who loan it money by deposit * * *. Such a power is a mere incident of the right to receive deposits, which by necessary implication gives power to assign and mortgage negotiable instruments as security for them * * *". *Morse on Banks and Banking (6 ed.), Vol. 1, sec. 63, p. 182.*

Another much-quoted text writer is of the same opinion:

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[1]Auten v. United States National Bank of New York, 174 U. S. 125, 141, 43 L. ed. 920, 926.

> "Of course, a pledge of assets in contemplation of insolvency for the sake of creating a preference is avoided by Section 5242 of the Revised Statutes (Title 12, U. S. C. A. sec. 91); but, in the absence of a preferential transfer in contemplation of insolvency, there is no federal statute under which a pledge of assets as security for a loan or deposit may be avoided". *Paton's Digest of Banking Law (1926), Vol 1, sec. 641.*

2. A solvent national bank, which has procured a railway company's deposit by furnishing at the bank's expense corporate surety bonds as security, has the power to pledge a portion of its assets, equivalent to that deposit, in lieu of those surety bonds, for the purpose of saving bond premiums, and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute company could not be obtained.

In support of this point your petitioner cites, without repeating, the authorities enumerated under its first proposition, and adopts as its argument the statements contained on uages 12 to 20 of the foregoing petition, being the second division of the reasons relied upon for an allowance of a writ of certiorari in this case.

3. A receiver of a national bank has no power to assert that a contract made by that bank for its benefit while solvent, is ultra vires.

Scott v. Armstrong, 146 U. S. 499, 510, 36 L. ed. 1059, 1063; Jones v. New York Guaranty & I. Co., 101 U. S.

622, 25 L. ed. 1030, 1035; Sioux City Terminal R. & Wareh. Co. v. Trust Co. of N. A., 173 U. S. 99, 110, 43 L. ed. 628, 632; Blair v. Chicago, 201 U. S. 400, 450, 50 L. ed. 801, 822.

Your petitioner adopts as its argument under this point the statements contained on page 19 of the foreing petition, being a portion of the second division of the reasons relied upon for an allowance of a writ of certiorari in this case.

4. A receiver of a national bank is estopped from asserting the want of power in that bank, while solvent, to pledge as security for a deposit a portion of its assets, equivalent to that deposit, in lieu of corporate surety bonds which the bank furnished, at its expense, to procure such deposit, when the substitution is made for the purpose of saving bond premiums and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute company could not be obtained, and when deposits have been made on the faith of the pledge agreement. *Chicago, R. I. & P. Co. v. Howard, 74 U. S. 392, 19 L. ed. 117, 121; Zabriskie v. Cleveland, C. & C. R. Co., 64 U. S. 381, 16 L. ed. 488, 498; Eastern Building & Loan Association v. Williamson, 189 U. S. 122, 129, 47 L. ed. 735, 741.*

Your petitioner adopts as its argument under this point, the statements contained on pages 18 to 20 of the foregoing petition, being a portion of the second divi-

sion of the reasons relied upon for the allowance of a writ of certiorari in this case.

5. A receiver of a national bank is estopped from asserting the want of power in that bank, while solvent, to pledge as security for a deposit a portion of its assets, equivalent to that deposit, after national bank examiners, who learned of the pledge agreement from the books of the bank before its failure, made no complaint of the transaction and by their silence permitted the depositor to make further substantial deposits.

In support of this point, your petitioner, without repeating, cites the authorities enumerated under its fourth proposition, and adopts the argument thereunder.

6. A pledge by a solvent national bank of a portion of its assets as security for a deposit which it desires to obtain or to retain is presumed to be valid, and this presumption will prevail in the absence of proof to the contrary. *Ohio & M. R. Co. v. McCarthy, 96 U. S. 258, 24 L. ed. 693, 695-696; Union Pacific R. Co. v. Chicago, R. I. & P. R. Co., 163 U. S. 564, 41 L. ed. 265.*

Your petitioner adopts as it sargument under this point, the statements contained on page 24 of the foregoing petition, being a portion of the third division of the reasons relied upon for an allowance of a writ of certiorari in this case.

7. When a solvent national bank induces a depositor to cancel and surrender corporate surety bonds protect-

ing its deposit and to accept in lieu thereof other security which the bank is without authority to furnish, moneys thereafter deposited in reliance upon that security are received by the bank as special deposits which it holds in trust for the use and benefit of the depositor, and those deposits, or their equivalent, may be recovered in full from the bank, or its receiver into whose hands they passed upon the bank's failure.

Your petitioner adopts as its argument under this point, the statements contained on page 23 of the foregoing petition, being a portion of the third division of the reasons relied upon for an allowance of a writ of certiorari in this case.

8. When a solvent national bank induces a depositor to cancel and surrender corporate surety bonds protecting its deposit and to accept in lieu thereof other security which the bank is without authority to furnish, the courts will enforce an implied agreement on the part of the bank to return the moneys deposited with it in reliance upon the invalid security, and those deposits never become general assets of the bank which its subsequently appointed receiver may distribute ratably among the bank's unsecured creditors. *Scott v. Armstrong, 146 U. S. 499, 507, 510, 36 L. ed. 1062-1063; Central Transportation Co. v. Pullman Car Co., 139 U. S. 24, 60, 35 L. ed. 55, 69; Aldrich v. Chemical National Bank, 176 U. S. 618, 636, 44 L. ed. 611, 618; Citizens' National Bank v. Appleton, 216 U. S. 196, 206, 54 L. ed. 443, 446.*

Your petitioner adopts as its argument under this point the statements contained on page 25 of the foregoing petition, being a portion of the third division of the reasons relied upon for an allowance of a writ of certiorari in this case.

Conclusion

It is respectfully submitted that the reasons assigned for an allowance of a writ of certiorari and the points of fact and law raised in petitioner's supporting brief sufficiently indicate the importance to the banking and business industries of an authoritative decision by the Supreme Court on each of the questions presented; and your petitioner prays that this Honorable Court will exercise its supervisory powers by granting a writ of certiorari in this case, and that the Court will review and upon final hearing reverse the decisions of the Circuit Court of Appeals and the trial court, and direct the entry of the judgment sought by your petitioner.

Dated at Dallas, Texas, June 1, 1933.

Respectfully submitted,

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Petitioner.

By T. D. Bruce
Of Counsel.

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CHARLES ELMORE

In the

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 128

THE TEXAS AND PACIFIC RAILWAY COMPANY,

Petitioner,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,

Respondent.

BRIEF OF THE TEXAS AND PACIFIC RAILWAY COMPANY

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Nov. 20, 1933.

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In the

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 128

THE TEXAS AND PACIFIC RAILWAY COMPANY,

Petitioner,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,

Respondent.

BRIEF OF THE TEXAS AND PACIFIC RAILWAY COMPANY

To the Honorable the Supreme Court of the United States:

Your petitioner's application for writ of certiorari to the Honorable Circuit Court of Appeals for the Fifth Circuit having been granted, this brief is filed pursuant to Rule 27.

Opinions in the Courts Below

The District Court did not write an opinion in the case. The opinion of the Circuit Court of Appeals is re-

ported in 63 Federal (2d) pages 1-5. The Circuit Court of Appeals on March 8, 1933, denied a petition for rehearing (R. 143), and your petitioner on June 6, 1933, filed its application for a writ of certiorari which this Honorable Court granted on October 9, 1933.

Grounds of Jurisdiction

(a) It is believed that the jurisdiction of this Honorable Court is sustained by section 347 of Title 28, United States Code (Judicial Code, section 240 as amended); also by *First National Bank v. Chicago T. & T. Co., 198 U. S. 280, 49 L. ed. 1051*, and *Texas & N. O. R. Co. v. Brotherhood Ry. & S. S. Clerks, 281 U. S. 548, 74 L. ed. 1034.*

(b) This case requires a construction of the National Bank Act of June 3, 1864 (Title 12, chap. 2, United States Code) and particularly that section of the Act providing that national banking associations organized thereunder "shall have power", inter alia,—

> "To exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this chapter" (12 U. S. C. A. §24, par. 7).

Specifically, this Honorable Court is requested to determine, among other things, whether or not (1) a solvent national bank, which has procured the account and deposits of a railroad company under an agreement to protect such account and deposits by corporate surety bonds, has the power to make a pledge of a portion of its assets in lieu of such bonds for the purpose of saving payment of premiums on the bonds and of retaining the account and deposits when one of the surety companies threatens withdrawal and a substitute surety can not be obtained; and (2) whether a receiver of that bank subsequently appointed by the Comptroller of the Currency may disaffirm such pledge agreement and retain both the pledged assets and the deposits although national bank examiners, who learned of the pledge agreement from the books of the bank one month before its failure, made no complaint of the transaction, and by their silence permitted the railway company thereafter to make substantial deposits upon the faith of the pledge agreement (R. 43-49, 88-95). The District Court by its judgment of May 26, 1932 (R. 39-42) and the Circuit Court of Appeals by its opinion and judgment of January 19, 1933 (R. 119-126) answered the first question negatively and the second question affirmatively, contrary, as your petitioner believes, to applicable decisions of this Honorable Court, and in a manner probably untenable or in conflict with the weight of authority.

Statement of the Case

The Texas and Pacific Railway Company is a corporation duly chartered and organized and now existing under and by virtue of the laws of the United States, to-wit: An Act of Congress entitled "An Act to incorporate the Texas Pacific Railroad Company, and to aid in the construction of its road, and for other purposes", approved March 3, 1871, and acts amendatory thereof and supplementary thereto, including an Act of Congress approved May 2, 1872, whereby, among other things, the name, style and title of said Texas and Pacific Railroad Company was changed to "The Texas and Pacific Railway Company" (R. 43, 88). Said railway company owns and operates in interstate and foreign commerce a line of railroad extending from New Orleans in the State of Louisiana to El Paso in the State of Texas over which a large volume of interstate traffic is constantly moving, and it is subject to all applicable provisions of the Interstate Commerce Act, as amended (R. 43-44, 88).

The defendant is the duly appointed, qualified and acting Receiver of The First National Bank of El Paso, Texas (R. 44).

The Texas and Pacific railway on July 3, 1922 was being operated by J. L. Lancaster and Charles L. Wallace, receivers appointed by the District Court of the

United States in and for the Western District of Louisiana, Monroe Division, and on that date, upon a petition filed by those receivers, an order was made and entered by that Court authorizing them to select The First National Bank of El Paso, Texas, as an additional depository for receivership funds. The order also recited that the bank "shall be required to furnish bonds with good and solvent sureties * * * in such an amount as will substantially equal the estimated average daily balances to be carried by said Receivers in said bank" (R. 44-45, 51-52, 88).

The First National Bank of El Paso, Texas, as principal, and National Surety Company, as surety, on or about July 10, 1922 executed and delivered to the receivers a surety bond for the sum of $25,000, conditioned as required by the Court's order, and thereupon the receivers opened an account with the bank and made deposits therein approximately in the amount of that surety bond (R. 45, 88).

The receivership of the Texas and Pacific railway was terminated on or about May 14, 1924, and upon the written request of the railway company, The First National Bank of El Paso, Texas, as principal, and National Surety Company, as surety, on or about August 7, 1924, executed and delivered to The Texas and Pacific Railway Company, and payable to it, a new surety bond for the sum of $25,000, conditioned in the same

manner as the old receivership bond, and guaranteeing that the bank,—

> "shall well and truly, on demand, pay over and deliver to The Texas and Pacific Railway Company, or its order, all and such sums of money, funds and valuables, general and special, as may now be on deposit by, in favor of, or in the name of The Texas and Pacific Railway Company with the said The First National Bank of El Paso, Texas, and as may be deposited hereafter by The Texas and Pacific Railway Company or by any one for its account, with the said The First National Bank of El Paso, Texas, or that may come into the custody or control of said The First National Bank of El Paso, Texas, for account of The Texas and Pacific Railway Company * * *" (R. 45, 54, 88).

The railway company's deposits with the bank increased during the month of April, 1927, and upon its written request, The First National Bank of El Paso, Texas, as principal, and Maryland Casualty Company, as surety, on or about April 25, 1927, executed and delivered to The Texas and Pacific Railway Company, and payable to it, an additional surety bond for the sum of $25,000, conditioned in the same manner as the bond next above quoted (R. 45-46, 55-56, 88).

During the month of January 1931, while the First National Bank was solvent and a going concern, its duly authorized active vice president-cashier called upon the

president of The Texas and Pacific Railway Company at Dallas, Texas, and requested him to accept as security for the railway company's deposits a pledge of United States Government Liberty Loan Bonds of the par value of $50,000 in lieu of the two $25,000 surety bonds. In explanation of this request, that bank officer stated that the First National desired to substitute the liberty bonds in order to relieve the bank of the premium payments on the surety bonds (R. 78-79, 89-90). Before making this trip to Dallas, the bank's vice president-cashier knew that the Maryland Casualty Company, surety on one of the $25,000 bonds, intended to "get off all bonds" of the First National Bank; that the bank was "going to have to give up this Maryland Casualty bond"; that the railway company was being asked to accept the liberty bonds in lieu of the surety bonds partly "because we knew eventually they (Maryland Casualty Company) would ask us to have the bond cancelled, or would not renew it"; and "I did not know when they withdrew we could not get any other surety company, any standard insurance company, to take that risk, but I had a good hunch". But this bank officer admitted that he "did not mention" to the railway company's president "at the time this substitution was made, or at any other time thereafter, this substitution was desired on account of the surety company threatening to cancel its bonds. He never heard of that, so far as I know" (R. 63, 70-72).

The railway president informed the vice president-cashier that it was the policy of the Texas and Pacific to require of depositories adequate security for its deposits, preferably corporate surety bonds; that the railway company would not continue its account with and make deposits in the First National Bank without security; that if the surety bonds were cancelled without the substitution of other adequate security the Texas and Pacific's account would be closed and its deposits withdrawn; but if the bank's officers and attorneys, after an investigation, concluded that the substitution of the liberty bonds in lieu of the surety bonds would be legal and valid in every particular, would constitute and be a binding and enforceable obligation against the bank, and would protect the railway company's deposits as fully and to the same extent as the surety bonds, the Texas and Pacific would agree to such substitution and to the cancellation of the surety bonds solely for the purpose of enabling the bank to save the bond premiums (R. 79-80, 90).

The bank's officer advised the president of the Texas and Pacific that the liberty bonds, when substituted for the corporate surety bonds, would protect the railway company's deposits as fully and to the same extent as they were then protected by corporate surety bonds and agreed to submit the proposed substitution

plan to the bank's attorneys for their investigation and approval (R. 90).

Thereafter, the vice president-cashier submitted the proposed substitution plan to the bank's attorneys, and after an investigation they advised the officers of the bank that the substitution could be legally made; that the pledge agreement would be an enforceable obligation against the bank; and that the substituted liberty bonds would protect the railway company's deposits as fully and to the same extent as the surety bonds. (R. 91).

At the request of the officers of the bank, its attorneys prepared a pledge agreement which was executed on January 29, 1931 in the regular course of the bank's business and while it was solvent by The First National Bank of El Paso, Texas, acting by and through F. M. Murchison, its president, and J. E. Benton, its cashier, which agreement recited in part:

> "For the purpose of securing the said Texas & Pacific Railway Company against any loss that might possibly occur by reason of its continuance and maintenance of the said deposit, The First National Bank of El Paso has on this date deposited in its Trust Department, and with its Trust Officer, which fact is evidenced by the signed statement to that effect of the said Trust Officer hereto attached, United States Government Liberty Bonds of the par value of Fifty Thousand ($50,000.00)

> Dollars, to be held by the said Trust Department, through its Trust Officer, in trust for the use and benefit of the said Texas & Pacific Railway Company. This is for the purpose of protecting it against loss as aforesaid, and it is agreed that the said Bonds shall, at all times, remain in the Trust Department as such security. * * *
>
> "Upon the closing of the said account, and only then, shall the said The First National Bank of El Paso have the right to withdraw the said securities from its Trust Department" (R. 91, 46-47, 57-58, 66).

Thereupon, the officers of the bank, while it was solvent and a going concern, with the full knowledge and approval of its board of directors, pursuant to said substitution agreement and in the regular course of the bank's business (R. 46, 66, 91), deposited in the Trust Department of the bank and with its Trust Officer, seven certain United States Government Fourth Liberty Loan 4-1/4 Coupon Bonds, 1933-38, of the aggregate amount and par value of $50,000, described by numbers and amounts as follows, to-wit:

G00129907	$ 5,000.00
A00115901	5,000.00
E00040105	5,000.00
K00129870	5,000.00
G00353057	10,000.00
H00353058	10,000.00
H 0029068	10,000.00.

The liberty bonds were so deposited with the Trust Officer separate and apart from all assets and securities of the bank and in a separate envelope bearing the name of The Texas and Pacific Railway Company, together with a copy of the pledge agreement and in accordance with the terms thereof (R. 46, 91-92); and the Trust Officer receipted for the bonds in the following language:

> "I, H. W. Moore, Trust Officer of the First National Bank of El Paso, hereby acknowledge receipt to the Trust Department of the said Bank of the Bonds above named and upon the conditions therein set forth" (R. 58-59).

All of those liberty bonds thereafter were held by said Trust Officer separate and apart from all assets and securities of The First National Bank of El Paso, Texas, and the liberty bonds for which the Texas and Pacific sued are the identical liberty bonds which were so deposited with the Trust Officer. A full record of this transaction was made upon the books of the bank on January 29, 1931, and those books ever since that date have reflected the same (R. 92).

The bank's vice president-cashier sent the executed pledge agreement to the president of the railway company at Dallas, Texas, and advised him that the officers and attorneys for the bank, after carefully investi-

gating the proposed substitution plan, had concluded that it would be in every respect a legal and binding obligation against the bank, that the pledge agreement had been prepared by the bank's attorneys, and that the bank's officers and attorneys were of the opinion and had declared that the executed pledge agreement and the liberty bonds, when substituted for the corporate surety bonds, would protect the deposits of The Texas and Pacific Railway Company in The First National Bank of El Paso, Texas, as fully and to the same extent as the corporate surety bonds (R. 92). Believing those representations to be true, the railway company's president accepted the executed pledge agreement and the liberty bonds, which had been placed in the custody of the bank's trust officer, in lieu of the then outstanding corporate surety bonds and caused the latter to be cancelled as of January 30, 1931 (R. 92-93). After the liberty bonds had been substituted for the surety bonds, The Texas and Pacific Railway Company, relying upon the pledge agreement and liberty bonds as security for its deposits, continued its account with and made deposits in The First National Bank of El Paso, Texas, and thereafter the railway company maintained in that bank an average daily deposit in excess of $50,000, the total par value of said liberty bonds; and the bank continued to accept and pay the railway company's checks and drafts drawn against its deposits until on

or about September 4, 1931, when the bank became insolvent, closed its doors to the public and refused to accept, honor or pay any other or further checks or drafts drawn by the railway company against its deposits (R. 47, 92-93, 63, 67, 81, 84-85).

The Texas and Pacific Railway Company deposited in the First National Bank during the period January 29, 1931 to August 5, 1931, a total of $132,220.27, and during the period August 6, 1931 to September 3, 1931, a total of $16,545.48. On the following dates it had on deposit the sums shown below, to-wit:

January 29, 1931	$22,264.10	
August 6, 1931	50,428.10	
September 3, 1931	54,646.94	(R. 93).

The First National Bank over a long period of years has furnished, often at its expense, corporate surety bonds to protect numerous deposits, both public and private, but apparently has not pledged its assets directly to private depositors for that purpose. By substituting the liberty bonds in lieu of the surety bonds as security for the railway company's deposits, the bank saved the premiums on the surety bonds, earned 4-1/4 per cent interest on the liberty bonds and was able to hold the railway company's account and deposits (R. 74, 94).

The Texas and Pacific Railway Company had $54,646.94 on deposit in the First National Bank on September 4, 1931, which sum of money it was entitled to receive from the bank upon demand. All of these funds, except accrued interest, were deposited by the railway company subsequent to January 29, 1931, the date on which the liberty bonds were substituted in lieu of the surety bonds as security for the Texas and Pacific's deposits, and all of those funds were collected by the railway company for common carrier services rendered in the transportation of both interstate and intrastate commerce (R. 48, 93).

The Comptroller of the Currency on or about September 6, 1931, duly and regularly appointed respondent S. O. Pottorff receiver of The First National Bank of El Paso, Texas, and on or about September 8, 1931, he took charge of the bank's affairs, assets and securities and its Trust Department in which the pledged liberty bonds were held as security for the railway company's deposits (R. 48, 88).[1]

National bank examiners acting under the supervision and control of the Comptroller of the Currency

[1] The receiver, pursuant to an agreement between the parties dated August 12, 1932 (R. 104), sold the liberty bonds for $52,273, which sum of money is being held by it "separate and apart from all assets" of The First National Bank of El Paso, Texas, "expressly subject to and for the purpose of satisfying any and all liens, claims or judgments which the Courts may adjudicate that The Texas and Pacific Railway Company has, or to which it may be entitled, in and to said liberty bonds, or the proceeds from the sale or sales thereof".

made an examination of the First National Bank commencing at 8 o'clock a. m. on August 6, 1931, and ending at noon on August 20, 1931, and their report to the Comptroller, covering the condition of the bank, forwarded after the bank closed, showed that liberty bonds of the par value of $50,000 were then pledged to secure the railway company's deposits (R. 94-95). They obtained this information from the books of the bank probably during the first two or three days of the examination. The officers of the bank were never notified or advised by either the bank examiners or the Comptroller of the Currency that the pledge of liberty bonds to secure the railway company's account was either irregular, illegal or beyond the powers of the bank, and no complaint of any character concerning the substitution agreement and the pledge of the liberty bonds was ever made to the bank's officers, or any of them, by the bank examiners or the Comptroller of the Currency (R. 94-95).

When the examination of the First National Bank began on August 6, 1931, the railway company had $50,428.10 on deposit, and between that date and September 3, 1931, the Texas and Pacific deposited an additional $16,545.48, relying upon the liberty bonds and the pledge agreement as security (R. 93-94).

The receiver allowed as a general claim only the Texas and Pacific's claim as a secured depositor for

the sum of $54,646.94, and tendered to the railway company a first dividend check for $16,394.08, being 30% of the full amount of its claim[1] (R. 94).

The Texas and Pacific Railway Company demanded of the receiver that he pay to it the sum of $54,646.94, which the receiver refused to do; the railway company then demanded that the receiver deliver to it the pledged liberty bonds and credit the company's claim with the market value of those bonds at the time of delivery, but this the receiver refused to do; and the railway company then demanded that the receiver sell the pledged liberty bonds and apply the proceeds of the sale to the liquidation of the company's claim, but the receiver refused to comply with this demand (R. 48-49, 88).

Thereupon, The Texas and Pacific Railway Company by its bill of complaint filed March 1, 1932, amended May 25, 1932, brought this action in the United States District Court for the Western District of Texas, El Paso Division, against S. O. Pottorff, Receiver of The First National Bank of El Paso, Texas, to recover of and from the receiver the liberty bonds pledged by the bank while solvent to secure the railway company's deposits, or to compel the receiver to sell those liberty bonds and deliver the proceeds of such sale to the railway company in partial settlement of its claim

1 Subsequent to the trial of this case the railway company, without prejudice to its rights, accepted the Comptroller's draft in the sum of $16,394.08 this reducing its claim as of September 4, 1931, to $38,252.86.

of $54,646.94 against the bank and its receiver; or, in the alternative, to compel the receiver to return to the railway company its deposits in the First National Bank as of September 4, 1931, or to recover of and from the receiver, as for money had and received, a sum of money equal to the railway company's deposits in the bank on that date (R. 1-20).

The receiver moved to dismiss the amended bill for want of equity and subsequent to that motion filed an answer alleging the invalidity of the pledge agreement. In addition, the receiver filed a cross-bill against the railway company seeking a judgment declaring the pledge agreement null and void, establishing the receiver's title to the liberty bonds and enjoining the railway company from asserting any rights thereto. To this cross-bill the Texas and Pacific filed a motion to dismiss for want of equity (R. 20, 21-27, 27-30, 31).

The trial court heard the case upon its merits and after argument overruled both motions to dismiss and rendered a decree on the cross-bill in favor of the receiver. From that decree the railway company prosecuted an appeal to the Circuit Court of Appeals for the Fifth Circuit, which Court on January 19, 1933, affirmed the decree of the trial court (R. 126) and on March 8, 1933, overruled the railway company's petition for a rehearing (R. 143).

Specifications of Error

The following specifications of error are based upon petitioner's assignments of error in the District Court (R. 108-113) and upon the errors assigned in its petition for rehearing in the Circuit Court of Appeals (R. 129-141).

I.

The Circuit Court of Appeals and the District Court erred in concluding and in holding as a matter of law that the bank's pledge of liberty bonds to secure the railway company's deposits was wholly void and of no effect.

II.

The Circuit Court of Appeals erred in its findings that the record is "devoid of affirmative proof that the thing the bank did here accords with national banking practices and customs, or is at all a necessary or desirable practice" (R. 120, 130).

III.

The Circuit Court of Appeals erred in its conclusions that the record does not "support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and neces-

sary to the proper conduct of the business of a national bank" (R. 124, 131).

IV.

The Circuit Court of Appeals erred in its finding and conclusion that the record "shows that with the same uniformity which has attended the recognition of the power of national banks to secure public deposits by pledge, the Comptroller has ruled that they may not do so in the case of private deposits" (R. 120-131).

V.

The Circuit Court of Appeals erred in holding that "the judicial knowledge of banking practices and customs which we may take establishes" that the giving of pledges for private deposits is not a reasonable incident to the business of receiving deposits and is not necessary to the proper conduct of the business of a national bank; and the Court further erred in basing its decision adverse to appellant in part upon such judicial knowledge (R. 124, 132).

VI.

The Circuit Court of Appeals erred in its holding that "a deposit is one thing, a loan another", and in rejecting "the view that implied authority to pledge assets as security for loans extends to pledging them to secure deposits" (R. 123-124, 132).

VII.

The Circuit Court of Appeals erred in holding that "generally speaking a bank's general powers do not authorize it to pledge assets for deposits", that the contract for security "was invalid because of want of power in the bank", that "this bank had no such power * * * because no express power to do so has been conferred upon it by statute", and because the record does not "support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" (R. 124, 125, 132-133).

VIII.

The Circuit Court of Appeals placed too heavy a burden of proof upon the railway company and particularly erred in holding, in effect, that to sustain the bank's implied power to make the pledge agreement, petitioner must affirmatively prove that such agreement was "necessary to the proper conduct of the business of a national bank" and "accords with national banking practices and customs" (R. 120, 124, 133).

IX.

The Circuit Court of Appeals erred in holding that [illegible] company "was as fully charged with knowledge [illegible] the bank was" of the latter's "want of power" to make the contract for security (R. 125, 133).

X.

The Circuit Court of Appeals and the District Court erred in concluding and in holding as a matter of law that the receiver may disaffirm the pledge agreement without returning or tendering back to the railway company the full amount of its deposits.

XI.

The Circuit Court of Appeals erred in holding and in applying to this case its ruling that "It is settled law in the courts of the United States that what a corporation cannot bind itself to do, the courts will not compel * * *; Especially will it not do it in a case of this kind, where the controversy is not between the bank and the railway, but between the railway and the bank's creditors, the bank having failed, and 'the interest of others than the parties' * * * being involved" (R. 125, 135-136).

XII.

The Circuit Court of Appeals erred in holding in effect that the receiver, as a representative of the bank's

creditors, has rights or equities in and to the pledged liberty bonds different from and superior to those of the bank before the receivership (R. 125, 135).

XIII.

Having found that the pledge agreement was wholly void and of no effect, the Circuit Court of Appeals and the District Court erred in concluding and in holding as a matter of law that the railway company's deposits made subsequent to the pledge of the liberty bonds were general deposits the title to which passed to the bank, and were not special deposits the title to which remained and now is in The Texas and Pacific Railway Company.

XIV.

Having found that the pledge agreement was invalid, the Circuit Court of Appeals erred in holding in effect that the agreement of deposit in this case definitely fixed the character of the deposit as general (R. 124, 125, 136-137).

XV.

The Circuit Court of Appeals erred in holding that the contract of deposit contained two agreements, viz: "One that the bank should pay back to the railway upon demand the sums deposited with it as other general de-

posits were. * * * The other is an agreement for security" (R. 124, 137).

XVI.

The Circuit Court of Appeals erred in holding "there is no basis at all here for declaring a trust," and in further holding, in effect, that the railway company, being a "general depositor" in the bank, cannot, because its security failed through an invalidity which in law it knew, have the bank converted into a trustee and itself into a cestui que trust of the money of the bank to the extent of the amount of its general deposit (R. 125-126, 137).

XVII.

The Circuit Court of Appeals and the District Court erred in concluding and in holding as a matter of law that the railway company is not entitled to recover of and from the bank's receiver a sum equal to the full amount of its deposits, plus interest, as for money had and received.

XVIII.

The Circuit Court of Appeals erred in disregarding appellant's alternative plea for money had and received and in holding that this is not a suit "on the

benefits received", but is a suit "upon a contract, to enforce it" (R. 125, 138).

XIX.

The Circuit Court of Appeals erred in its conclusion that "this is not a case" like that "of a solvent bank which has obtained the benefit of a transaction, seeking to avoid, on the ground of ultra vires, returning what it has received" (R. 125, 134-135).

XX.

The Circuit Court of Appeals erred in holding in effect that the case at bar is one "not between the bank and the railway, but between the railway and the bank's creditors" (R. 125, 135).

Summary of Argument

Petitioner's argument is distributed under the following propositions, viz.:

1. A solvent national bank has the power to pledge, as security for deposits which it desires to procure or retain, a portion of its assets equivalent in amount to those deposits.

2. A solvent national bank, which has procured a railway company's deposits by furnishing at the bank's expense corporate surety bonds as security, has the power to pledge a portion of its assets, equivalent in amount to those deposits, in lieu of the surety bonds, for the purpose of saving bond premiums, and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute surety company cannot be obtained.

3. A pledge by a solvent national bank of a portion of its assets as security for deposits which it desires to procure or retain is presumed to be valid, and this presumption will prevail in the absence of proof to the contrary.

4. The Receiver of The First National Bank of El Paso, Texas, has no power to question the validity of the pledge agreement.

5. The receiver of a national bank is estopped from asserting the want of power in that bank, while solvent, to pledge as security for deposits a portion of its assets, equivalent in amount to those deposits, in lieu of corporate surety bonds, which the bank furnished at its expense to procure such deposits, when the substitution was made for the purpose of saving bond premiums and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute surety company could not be obtained, and when deposits have been made on the faith of the pledge agreement.

6. The receiver of a national bank is estopped from asserting the want of power in that bank, while solvent, to pledge as security for deposits a portion of its assets, equivalent in amount to those deposits, after national bank examiners, who learned of the pledge agreement from the books of the bank a month before its failure, made no complaint of the transaction and by their silence permitted the depositor to make further substantial deposits in reliance upon the pledge agreement.

7. When a solvent national bank induces a depositor to cancel and surrender corporate surety bonds protecting its deposits and to accept in lieu thereof other security which the bank is without authority to furnish, moneys thereafter deposited in reliance upon that security are received by the bank as special de-

posits which it holds in trust for the use and benefit of the depositor, and those deposits, or an equivalent sum of money, may be recovered in full from the bank or from its receiver into whose hands they passed upon the bank's failure.

8. When a solvent national bank induces a depositor to cancel and surrender corporate surety bonds protecting its deposits and to accept in lieu thereof other security which the bank is without authority to furnish, the courts will enforce an implied agreement on the part of the bank to return the moneys deposited with it in reliance upon the invalid security, and those deposits never become general assets of the bank which its subsequently appointed receiver may distribute ratably among the bank's unsecured creditors.

For convenience we have grouped for argument propositions 1, 2 and 3, infra pages 34-35, propositions 4, 5 and 6, infra pages 58-59, and propositions 7 and 8, infra page 75.

Under propositions 1, 2 and 3 petitioner argues that a solvent national bank has power to pledge a portion of its assets as security for deposits, either public or private, which it desires to procure or retain, and that it has power to pledge a portion of its assets as security for such deposits in lieu of corporate surety bonds, on which the bank pays the premiums,

for the purpose of saving those premiums and affording adequate security due to the threatened withdrawal of a surety company for which a substitute surety company cannot be obtained. Among other things it is shown:

(a) There is no statutory prohibition against solvent national banks pledging a portion of their assets to secure deposits.

(b) National banking associations are authorized in section 24 of the National Bank Act to exercise all such incidental powers as shall be necessary to carry on the business of banking, including that of receiving deposits.

(c) The incidental powers granted to national banks in section 24 of the National Bank Act are not restrictions upon but are additions to the express powers granted in that section.

(d) The word "necessary" as used in section 24 of the National Bank Act means "convenient" or "useful", and national banks may exercise such incidental powers as shall be convenient or useful in carrying on the business of banking, including that of receiving deposits.

(e) The pledge of liberty bonds in lieu of corporate surety bonds in the case at bar was both convenient

and useful to the First National Bank. By that substitution the bank saved the premiums on surety bonds, earned 4-1/4 per cent interest on the liberty bonds, was able to hold the railway company's account and deposits, and thereafter received from the railway company deposits totaling $148,765.75.

(f) This Honorable Court has held that national banks may pledge their assets as security for loans, also, that a deposit is a loan; therefore, those banks may pledge their assets as security for deposits.

(g) Text writers recognize the power of solvent national banks to pledge a portion of their assets as security for deposits which they wish to procure or retain.

(h) The United States Attorney General has held that the power to receive deposits is indispensable to the conduct of the business of banking; that the extent of its exercise is in a degree the measure of the success of banks; that national banks may give security for deposits and that the means of securing them are not limited or restricted by statute but rest in the discretion of the bank's officers and directors.

(i) The Honorable Circuit Court of Appeals for the Fourth Circuit has affirmed the power of solvent national banks to pledge portions of their assets as security for deposits, and has recognized their power

to substitute a pledge of assets in lieu of corporate surety bonds for the purpose of saving bond premiums.

(j) A substitution of a pledge of assets in lieu of corporate surety bonds for the purpose of saving bond premiums is a compromise arrangement for the benefit of the bank and is within its incidental powers.

(k) This Honorable Court has held that the provisions of the National Bank Act are not directed against all pledges whereby one creditor may obtain greater payment than another but against those given or arising after or in contemplation of insolvency; further, that liens, equities and rights arising by express agreement, or implied from the dealings between the parties, or by operation of law, prior to insolvency and not in contemplation thereof, are not invalidated. In the case at bar the pledge agreement was made while the bank was solvent and a going concern, and seven months before its failure.

(l) The Comptroller of the Currency has not ruled that national banks have no power to pledge their assets as security for deposits; on the contrary, national bank examiners appointed by the Comptroller, who learned of the pledge of liberty bonds in this case about one month before the bank failed, made no complaint to the officers of the bank and by their

silence permitted the railway company thereafter to make deposits totaling $16,545.48 in reliance upon the pledge agreement.

(m) The incidental powers conferred upon national banking associations by section 24 of the National Bank Act are not restricted to those acts or transactions which accord with national banking practices and customs; on the contrary, national banks are empowered to exercise all such incidental powers as shall be convenient or useful in carrying on the banking businesses specified in section 24, including that of receiving deposits.

(n) A party relying upon the power of a national bank to pledge a portion of its assets in lieu of corporate surety bonds as security for deposits need only prove that the pledge was made while the bank was solvent, that it was convenient or useful to the bank and in furtherance of the express power to receive deposits; when this showing has been made, as was done in the case at bar, the transaction, in the absence of proof to the contrary, is presumed to be valid.

The argument under propositions 4, 5 and 6 covers three principal points, namely:

(1) The Receiver of the First National Bank of El Paso, Texas, has no authority to question the validity

of the pledge agreement; he acquired no greater rights to or equities in the pledged liberty bonds than those possessed by that bank before its insolvency.

(2) The pledge of liberty bonds by the First National Bank was not an *ultra vires* act as those acts have been defined in decisions of this Honorable Court; in making the pledge the bank was carrying out an express power to receive deposits.

(3) The receiver is estopped from questioning the validity of the pledge agreement without returning or tendering to the railway company the deposits made by it in reliance upon that agreement as security, especially since national bank examiners, appointed by the Comptroller, learned of the pledge agreement one month before the bank failed but made no complaint to the bank's officers and by their silence permitted the railway company thereafter to make additional deposits totaling $16,545.48 in reliance upon that agreement.

Under propositions 7 and 8 petitioner contends that, if the pledge agreement be null and void, the bank received the railway company's deposits not as general but as special deposits, the title to which remained in the railway company; that those deposits passed to the receiver as a part of the so-called "as-

sets" of the bank; and that those assets are impressed with a trust in favor of the railway company to the extent of its deposits.

If this Honorable Court should hold, as did the Circuit Court of Appeals, that the amended bill of complaint sets forth only a cause of action upon the pledge agreement, and if this Court should hold that such agreement is *ultra vires* and void and may be disaffirmed by the receiver, petitioner asks that such action of the Court be without prejudice to another cause of action by petitioner against the receiver for money had and received or for the recovery of or compensation for the money with which petitioner parted on the faith of the pledge agreement.

ARGUMENT

First, Second and Third Propositions

1. A solvent national bank has the power to pledge, as security for deposits which it desires to procure or retain, a portion of its assets equivalent in amount to those deposits.

2. A solvent national bank, which has procured a railway company's deposits by furnishing at the bank's expense corporate surety bonds as security, has the power to pledge a portion of its assets, equivalent in amount to those deposits, in lieu of the surety bonds, for the purpose of saving bond premiums, and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute surety company cannot be obtained.

New York County National Bank v. Massey, 192 U. S. 138, 145, 48 L. ed. 380, 383; Marine Bank v. Fulton County Bank, 69 U. S. 252, 17 L. ed. 785, 787; Auten v. United States National Bank of New York, 174 U. S. 125, 43 L. ed. 920, 926; Aldrich v. Chemical National Bank, 176 U. S. 618, 626, 44 L. ed. 611, 614; Wyman v. Wallace, 201 U. S. 230, 243, 50 L. ed. 738, 742; Jacksonville, Mayport, Pablo R. & Nav. Co. v. Hooper, 160 U. S. 514, 525, 40 L. ed. 515, 523; Ohio & M. R. Co. v. McCarthy, 96 U. S. 258, 24 L. ed. 693, 695-696; Union Pacific R. Co. v. Chicago, R. I. & P. R. Co., 163 U. S. 564, 581, 41 L. ed. 265, 271; Pittsburgh, C. &

St. L. R. Co. v. Keokuk & H. Bridge Co., 131 U. S. 371, 384-385, 33 L. ed. 157, 161-162; McCullough v. Maryland, 4 Wheaton 316, 412-414, 4 L. ed. 579, 603; First National Bank of Charlotte v. National Exchange Bank of Baltimore, 92 U. S. 122, 23 L. ed. 679, 681; Head v. The University, 86 U. S. 526, 22 L. ed. 160; Scott v. Armstrong, 146 U. S. 499, 510, 36 L. ed. 1059, 1063.

3. A pledge by a solvent national bank of a portion of its assets as security for deposits which it desires to procure or retain is presumed to be valid, and this presumption will prevail in the absence of proof to the contrary.

Ohio & M. R. Co. v. McCarthy, 96 U. S. 258, 24 L. ed. 693, 695-696; Union Pacific R. Co. v. Chicago, R. I. & P. R. Co., 163 U. S. 564, 41 L. ed. 265.

Argument Under First, Second and Third Propositions

The Honorable Circuit Court of Appeals for the Fifth Circuit has held that "generally speaking a bank's general powers do not authorize it to pledge assets for deposits" and that The First National Bank of El Paso, Texas, "had no such power" (R. 124). This conclusion was reached "not because the recognition of the power would conflict with our views of public policy" (R. 124), but because, as stated by the Court:

(1) "no express power to do so has been conferred upon it by statute" (R. 124);

(2) "no single other instance of the practice having been indulged in has been presented" (R. 120);

(3) the record "shows that with the same uniformity which has attended the recognition of the power of national banks to secure public deposits by pledge, the Comptroller has ruled that they may not do so in the case of private deposits" (R. 120);

(4) "a deposit is one thing, a loan another" and "the implied authority to pledge assets as security for loans" does not extend "to pledging them to secure deposits" (R. 123, 124);

(5) the record is "devoid of affirmative proof that the thing the bank did here accords with national banking practices and customs, or is at all a necessary or desirable practice" (R. 120);

(6) "the record does not support the finding necessary to be made if the power is implied, that the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits, and necessary to the proper conduct of the business of a national bank" and "the judicial knowledge of banking practices and customs which we may take establishes the contrary to be true" (R. 124).

Thus we have a composite picture of the mind of the Circuit Court of Appeals on the question of power. But that Court made no effort to explain or define the language of section 24 of the National Bank Act which provides that a national banking association "shall have power * * * to exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; * * * by receiving deposits * * *". We momentarily defer a consideration of this language to dispose of certain propositions next above enumerated.

The Circuit Court of Appeals erred in finding (R. 120) that the record does not disclose a single other instance of a national bank pledging part of its assets to secure a deposit. The case of *Baltimore & Ohio Railway Company v. Smith, 56 Fed. (2d) 799,* is another instance, and the judgment of the District Court below was predicated upon the decision in that case (R. 34). *Illinois Central Railroad Company v. A. F. Rawlings, Receiver,* now pending before this Honorable Court on petition for writ of certiorari to the Honorable Circuit Court of Appeals for the Fifth Circuit, is another instance of a bank securing a deposit by a pledge of assets.

The Circuit Court of Appeals erred in finding that the record shows the Comptroller has uniformly ruled that national banks may not pledge part of their as-

sets to secure private deposits (R. 120). There is nothing in the record to warrant this finding; in fact the receiver offered no evidence upon the trial of the case (R. 88). To the contrary, the record does show that national bank examiners, appointed by the Comptroller, during an examination of the books of the First National Bank about one month before its failure, learned of the pledged liberty bonds, but they did not notify the officers of the First National Bank that the pledge agreement was either irregular, illegal or beyond the powers of the bank, and no complaint of any character concerning the substitution agreement and the pledge of the liberty bonds was ever made to the officers of the bank, or any of them, by those bank examiners or the Comptroller of the Currency (R. 94, 95). If, as stated by the Circuit Court of Appeals, the Comptroller has uniformly ruled that national banks may not pledge their assets to secure private deposits, it is strange indeed that the Comptroller's agents would be so derelict in their duties as to say nothing about such a "reprehensible" transaction when it came to their notice.

The Circuit Court of Appeals, following the Supreme Court of Arkansas in *McCown v. Edwards, 48 S. W. (2d) 558*, erroneously held that "a deposit is one thing, a loan another" and "the implied authority to pledge assets as security for loans" does not extend "to pledging them to secure deposits" (R. 123, 124). The rela-

tionship between a bank and its depositors often has been stated by this Honorable Court. Thus:

New York County National Bank v. Massey, 192 U. S. at page 145, 48 L. ed. p. 383 (quoting from Davis v. Elmira Savings Bank, 161 U. S. 275, 288):

> "'The deposit of money by a customer with his banker is one of loan, with the superadded obligation that the money is to be paid, when demanded, by a check' ".

Auten v. United States National Bank, 174 U. S. at pages 141-142, 43 L. ed. p. 926:

> "Banking in much, if not in the greater part of its practice, is in strict sense borrowing, and we may well hesitate to condemn it as illegitimate, or regard it as out of the course of regular business, and hence suspicious and questionable".

Marine Bank v. Fulton County Bank, 69 U. S. at page 256, 17 L. ed. 787:

> "All deposits made with bankers may be divided into two classes, namely: those in which the bank becomes bailee of the depositor, the title to the thing deposited remaining with the latter; and that other kind of deposit of money peculiar to banking business, in which the depositor, for his own convenience, parts with the title to his money and

> loans it to the banker; and the latter, in consideration of the loan of the money and the right to use it for his own profit, agrees to refund the same amount, or any part thereof on demand".

Furthermore, while recognizing that the power to borrow money "is not expressly given by the (national bank) act", this Honorable Court nevertheless has upheld pledges of assets to secure such loans because a national bank has the implied power "to incur liabilities in the regular course of its business," *Aldrich v. Chemical National Bank, 176 U. S. at page 626, 44 L. ed p. 614,* and because "it is not in terms prohibited by the National Banking Act," *Wyman v. Wallace, 201 U. S. at page 243, 50 L. ed. p. 742.* Since a deposit is a loan and a loan may be secured by a pledge of assets it follows that deposits may be so secured.

Morse on Banks and Banking (6 ed.), Vol. 1, §63, p. 182:

> "A bank may secure persons who loan it money by deposit * * *. Such a power is a mere incident of the right to receive deposits, which by necessary implication gives power to assign and mortgage negotiable instruments as security for them * * *".

Paton's Digest of Banking Law (1926), Vol. 1, §641:

> "Of course, a pledge of assets in contemplation of insolvency for the sake of creating a preference

> is avoided by Section 5242 of the Revised Statutes (Title 12, U. S. C. A. §91); but, in the absence of a preferential transfer in contemplation of insolvency, there is no federal statute under which a pledge of assets as security for a loan or deposit may be avoided."

The absence of express statutory power to pledge a part of its assets to secure deposits does not mean that national banks, while solvent, do not possess implied power so to do. Such implied power is clearly conferred by section 24 of the National Bank Act which provides that national banking associations "shall have power",—

> "To exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this chapter" (12 U. S. C. A. §24, par. 7).

After quoting the foregoing paragraph, this Honorable Court, in *First National Bank of Charlotte v. Na-*

tional Exchange Bank of Baltimore, 92 U. S. at page 127, 23 L. ed. p. 681, stated:

> "Authority is thus given to transact such a banking business as is specified, and all incidental powers necessary to carry it on are granted".

Congress having specifically declared that the receiving of deposits is a banking business, it follows that national banks may exercise all incidental powers necessary to receive deposits. We are thus brought to a definition of the word "necessary" as here employed.

It is perfectly plain that the Honorable Circuit Court of Appeals placed the strictest possible interpretation upon the word "necessary", evidently taking it for granted that the lawmakers used it as a synonym of the word "indispensable", but such was not their intention. As far back as *McCullough v. Maryland, 4 Wheaton 316, 412, 4 L. ed. 579, 603,* Chief Justice Marshall, in affirming the incidental power of the Federal Government to incorporate a national bank, placed a different interpretation upon a similar use of that word. We quote from that decision:

> "To its (the constitution's) enumeration of powers is added that of making 'all laws which shall be *necessary* and proper, for carrying into execution the foregoing powers, and all other powers vested by this constitution, in the Government of the

United States, or in any department thereof" (Wheat. pp. 412-13, L. ed. pp. 602-603).

* * * * *

"The argument on which most reliance is placed, is drawn from the peculiar language of this clause. Congress is not empowered by it to make all laws, which may have relation to the powers conferred on the government, but such only as may be '*necessary* and proper' for carrying them into execution. The word '*necessary*' is considered as controlling the whole sentence, and as limiting the right to pass laws for the execution of the granted powers, to such as are *indispensable*, and without which the power would be nugatory. That it excludes the choice of means, and leaves to Congress, in each case, that only which is most direct and simple.

"Is it true that this is the sense in which the word '*necessary*' is always used? Does it always import an absolute physical necessity, so strong that one thing, to which another may be termed necessary, cannot exist without that other? We think it does not. If reference be had to its use, in the common affairs of the world, or in approved authors, we find that it frequently imports no more than that one thing is *convenient*, or *useful*, or essential to another. To employ the means necessary to an end, is generally understood as employing any means calculated to produce the end, and not as being confined to those single means, without which the end would be entirely unattainable. Such is the character of human language, that no word conveys to the mind, in all situations, one single definite idea; and nothing is more common than to use words in a figurative sense. Almost all

> compositions contain words, which, taken in their rigorous sense, would convey a meaning different from that which is obviously intended. It is essential to just construction, that many words which import something excessive should be understood in a more mitigated sense—in that sense which common usage justifies. The word *'necessary'* is of this description" (our italics) (Wheat. pp. 412-414, L. ed. p. 603).

It should be presumed, at least in absence of proof to the contrary, that Congress in drafting section 24 of the National Bank Act, used the word "necessary" in its liberal sense and intended it to convey the meaning ascribed to it by this Honorable Court in *McCullough v. Maryland*, supra. Employing this definition and applying it to the foregoing quotation from *First National Bank of Charlotte v. National Exchange Bank of Baltimore*, we find that the power conferred upon national banks was two-fold: (1) "To transact such a business as is specified", i. e. the business of "receiving deposits"; and (2) "all such incidental powers necessary", i. e. convenient, useful, or essential, "to carry it on", i. e. the business of procuring deposits, and securing them, "are granted". It should be observed that the implied power thus granted, to use other language of Chief Justice Marshall, "is placed among the powers * * *, not among the limitations on those

powers. Its terms purport to enlarge, not to diminish the powers. It purports to be an additional power, not a restriction on those already granted" (4 Wheat. 419-420, 4 L. ed. 604-605). However, the Act requires those implied powers to be exercised "subject to law", which term this Honorable Court, in *Head v. The University, 86 U. S. at page 530, 22 L. ed. p. 160*, has defined to mean "subject to whatever law" the legislative body "might think fit to pass". But we find nothing in the National Bank Act prohibiting national banks, while solvent, from pledging a part of their assets to procure or retain deposits. We do find that Congress declared in section 52 of the Act of 1864 (12 U. S. C. A. §91) that,—

> "All transfers of the notes, bonds, bills of exchange, or other evidences of debt owing to any national banking association, or of deposits to its credit; all assignments of mortgages, sureties on real estate, or of judgments or decrees in its favor; all deposits of money, bullion, or other valuable thing for its use, or for the use of any of its shareholders or creditors; and all payments of money to either, made after the commission of an act of insolvency, or in contemplation thereof, made with a view to prevent the application of its assets in the manner prescribed by this chapter, or with a view to the preference of one creditor to another, except in payment of its circulating notes, shall be utterly null and void * * *".

The plain implication of this statute is that transfers made before the commission of an act of insolvency and not in contemplation thereof shall be valid and enforceable,—such as the pledge of liberty bonds in the case at bar.

If a bank be solvent, there can be no valid objection to its giving in good faith a dollar security for a dollar gained by deposit, for the bank at any time can fully discharge all of its obligations. Hence it was that Congress limited its prohibition to transfers made by banks while insolvent or in contemplation thereof, fully understanding and intending that the quoted section would afford all the protection to which the bank's creditors should be entitled.

This interpretation of the Act is confirmed by the following statement of this Honorable Court in *Scott v. Armstrong, 146 U. S. at page 510, 36 L. ed. p. 1063:*

> "Undoubtedly any disposition by a National Bank, being insolvent or in contemplation of insolvency, of its choses in actions, securities or other assets, made to prevent their application to the payment of its circulating notes, or to prefer one creditor to another, is forbidden; but liens, equities or rights arising by express agreement, or implied from the nature of the dealings between the parties,

> or by operation of law, prior to insolvency and not in contemplation thereof, are not invalidated. The provisions of the Act are not directed against all liens, securities, pledges or equities, whereby one creditor may obtain a greater payment than another, but against those given or arising after or in contemplation of insolvency".

The pledge agreement in the case at bar was made for the benefit of the bank (R. 90, 94) in the regular course of its business (R. 66) and while it was solvent and a going concern (R. 46, 89, 91).

Attorney General T. W. Gregory, in an opinion furnished the Secretary of the Treasury on March 31, 1915, held that a national bank had the implied power to "enter into a contract with a guaranty company under which, in consideration of premiums paid by the bank, the company 'insures and guarantees each depositor in the bank the full payment of his deposit therein' " (30 Op. 341). In reaching this conclusion, the Attorney General said in part:

> "The law confers upon national banks such incidental powers as are required to meet all legitimate demands of the banking business and to enable them to conduct their affairs safely and prudently within the scope of their charters. (Sec. 5136, Rev. Stat.; First National Bank v. National Exchange Bank, 92 U. S. 122, 127.) The power to give security for deposits seems to be recognized by section

5153, Revised Statutes, as among these incidental powers. The section last mentioned, after providing that all associations created under the act shall, when so designated by the Secretary of the Treasury, be depositories, further provides that 'The Secretary of the Treasury shall require the associations thus designated to give satisfactory security, by the deposit of United States bonds and otherwise, for the safe-keeping and prompt payment of the public money deposited with them,' etc. It is believed that this section is more reasonably construed as a recognition of the existence of the power on the part of national banks to give security for deposits than as a grant by implication of authority to give security for Government deposits alone.

"The power of banks to give security for deposits or for payment of their debts has been frequently recognized. It has been held that the property of a bank may be pledged as security for a debt (United States v. Robertson (1831), 5 Pet. 611, 650); that a bond with sureties may be given to prevent depositors from withdrawing their accounts (Wylie v. Commercial & Farmers' Bank (1902), 41 S. E. 504, 509, 63 S. C. 406), and that a national bank may give its bond with sureties to secure a deposit of State funds (State of Nebraska v. First National Bank of Orleans (1898); 88 Fed. 947, 951.)

"The power to contract for guaranteeing or securing depositors arises from the nature of the relation existing between the banks and their depositors. The relation created between the bank and a depositor by the receipt of deposits is that of debtor and creditor. (Bank of the Republic v. Millard (1869); 10 Wall. 152, 155; Davis v. Elmira Savings Bank (1896), 161 U. S. 275, 288). The

power to receive deposits, expressly granted to every national bank (sec. 5136 R. S.), is, of course, indispensable to the conduct of the business of banking, and the extent of its exercise is in a degree the measure of the success of the bank. * * *

"The means by which depositors are to be protected and secured are not expressly limited or restricted by statute. A large discretion is left to the officers and directors. They may use such means for the purpose as are not prohibited by, or inconsistent with the provisions of, the law, and as they may reasonably find to be suitable and proper and not inconsistent with the prudent conduct of the affairs of the bank within the scope of its charter. * * *"

The Honorable Circuit Court of Appeals for the Fourth Circuit is of the same opinion. In *Burrowes v. Nimocks, 35 Fed. (2d) 152*, Circuit Judge Parker thus stated that case:

"This was a suit instituted by the receiver of the National Bank of Fayetteville, N. C., against the treasurer of Cumberland county, N. C., to determine the right to certain notes which had been transferred by the bank to the treasurer as security for the deposit of county funds" (p. 153).

In dealing with the receiver's contention that the vice president of the bank had no authority to secure the deposit, which the Court found to be in the nature

of a call loan and which the laws of North Carolina required to be secured, Judge Parker stated:

> "The vice president was expressly authorized to seek it (the deposit); and this authority carried by necessary implication the power to give the security necessary to obtain it" (p. 154).

While it is true that county funds were secured in the Nimocks case, the security was given prior to the 1930 amendment to the National Bank Act which specifically authorized national banks to give security for deposits of States and their political subdivisions in accordance with respective State laws, hence the question before the Court was one of implied power, under section 24 of the National Bank Act, to secure those funds, and the case therefore was essentially similar to the case at bar. Furthermore, there is no valid distinction between the giving of security for a public and a private deposit. As stated by Circuit Judge Parker in *Schumaker v. Eastern Bank & Trust Co., 52 Fed. (2d) 925:*

> "Whether a bank may pledge its assets for the security of an ordinary depositor is a question as to which there is conflict of authority. For cases denying such power, see Smith v. B. & O. R. Co. (D. C.), 48 F. (2d) 861; Divide County v. Baird, Receiver, 55 N. D. 45, 212 N. W. 236, 51 A. L. R. 296; Farmers' & Merchants' State Bank v. Consolidated School District, 174 Minn. 286, 219 N. W.

163, 65 A. L. R. 1407. For cases asserting it, see Ward v. Johnson, 95 Ill. 215; Ahl v. Rhoads, 84 Pa. 319; Cameron v. Christy, 286 Pa. 405, 133 A. 551; Richards v. Osceola Bank, 79 Iowa 707, 45 N. W. 294; McFerson v. National Surety Co., 72 Colo. 482, 212 P. 489; Ex Parte Grand Lodge, C. U. O. O. F. (State ex rel. Bradley v. People's Federation Bank), 147 S. C. 103, 144 S. E. 841; Williams v. Hall, 30 Ariz. 581, 249 P. 755; Grigsby v. People's Bank, 158 Tenn. 182, 11 S. W. (2d) 673. And as bearing on the question generally, see notes in 51 A. L. R. 313, and 65 A. L. R. 1412. Although some of the cases draw a distinction between a pledge of assets to secure a deposit of public funds and a pledge to secure a private deposit, there would seem to be, in the absence of statute, no valid basis for such distinction; * * *".

In determining whether or not the First National Bank had the implied power to substitute a pledge of assets in lieu of corporate surety bonds upon which it was paying premiums, this Honorable Court should have these facts in mind: Although admittedly solvent (R. 46, 89), it became necessary for the First National Bank to curtail expenses, including the premiums which it had been paying on the surety bonds protecting the railway company's deposits (R. 64). In addition, the Maryland Casualty Company, surety on one of those $25,000 bonds, had informed the officers of the bank that it was "going off" all bonds, and it was apparent

the bank would experience difficulty in procuring a substitute surety company (R. 70-72). The bank's officers knew that the railway company, with the cancellation of its bonds, would close its account and withdraw its deposits (R. 90), and this it wished to avoid. Being unware of the action of the Maryland Casualty Company (R. 72), the railway company, solely for the purpose of aiding the bank (R. 90), accepted the proffered pledge of liberty bonds, authorized the cancellation of its surety bonds (R. 92-93), continued its account with the First National Bank and thereafter deposited with it a total of $148,765.75 in reliance upon the pledge agreement (R. 93). The substitution of liberty bonds for corporate surety bonds was made in the regular course of the bank's business (R. 66) and while the bank was solvent and a going concern (R. 46, 89, 91). By this substitution the bank saved the premiums on the surety bonds, earned 4-1/4 per cent interest on the liberty bonds, and was able to hold the railway company's account and deposits (R. 94.)

It is clear that these facts bring this case within the rule announced by Judge Parker in *Burrowes v. Nimocks*, supra, namely, that the pledging of a bank's securities as protection for a deposit for the purpose of saving bond premiums is a reasonable exercise of the authority of a bank's vice president to procure such de-

posit [35 Fed. (2d) at page 154] and within the principle announced by this Honorable Court in *First National Bank of Charlotte v. National Exchange Bank of Baltimore, 92 U. S. 122, 23 L. ed. p. 679.* In that case it was held that the implied powers granted in section 24 of the National Bank Act "are such as are required to meet all the legitimate demands of the authorized business, and to enable a bank to conduct its affairs, within the general scope of its charter, safely and prudently". In this connection the Court said:

> "This necessarily implies the right of a bank to incur liabilities in the regular course of its business, as well as to become the creditor of others. Its own obligations must be met, and debts due to it collected or secured. The power to adopt reasonable and appropriate measures for these purposes is an incident to the power to incur the liability or become the creditor. Obligations may be assumed that result unfortunately. Loans or discounts may be made that cannot be met at maturity. Compromises, to avoid or reduce losses, are oftentimes the necessary results of this condition of things. These compromises come within the general scope of the powers committed to the Board of Directors and the officers and agents of the bank, and are submitted to their judgment and discretion, except to the extent that they are restrained by the charter or by-laws. Banks may do, in this behalf, whatever natural persons could do under like circumstances" (L. ed. p. 681).

What the bank did in the case at bar amounted to a compromise. It had procured the account and deposits of the railway company by furnishing corporate surety bonds on which it paid the premiums. These payments became burdensome and the bank wished to be relieved of them. At the same time the bank wished to retain the railway company's account and deposits which were beneficial to it. The bank's officers conceived the idea of effecting a compromise through the substitution of a pledge of a portion of the bank's assets in lieu of the surety bonds. By doing this the bank would be able to keep the railway company's account, which carried an average daily deposit balance of approximately $50,000, and at the same time save the bond premiums. This the bank clearly had authority to do.

We respectfully submit that these record facts clearly show that the pledging of assets in lieu of corporate surety bonds by the First National Bank was, contrary to the holding of the Circuit Court of Appeals (R. 121, 124), both "necessary" (as that word has been defined by this Honorable Court) and desirable, and that it was "a reasonable incident to the business of receiving deposits."

The National Bank Act does not require every act of a national bank to "accord with national banking practices and customs" before such act is legal. Neither does

it prohibit the doing of a certain act unless that act first is shown to be "necessary (that is, indispensable) to the proper conduct of the business of a national bank". Those banks are authorized to exercise all incidental powers which are convenient or useful (if not prohibited) in carrying on the business of banking, which includes the business of receiving deposits. A transaction, therefore, which comes within this implied power is valid even when performed for the first time by a national bank. And it is manifestly improper for the Courts, as was done in this case, to place a burden of proof upon petitioner greater than the Act itself required. If the railway company had any burden of proof it was merely to show, as it did, that the pledging of the bank's assets in lieu of corporate surety bonds was done at the special instance and request of the bank, in the regular course of its business, while the bank was a solvent and going concern, and several months before any question of the solvency of the bank arose, and that the pledging of the assets was convenient and useful to the bank, and resulted in a distinct advantage to it. Certainly these facts raised a presumption in favor of the validity of the pledge under the rule announced by this Honorable Court to the effect that corporations are presumed to contract within their powers, and, in the absence of proof to the contrary, their contracts are presumed to

be valid when not foreign to the purposes for which the corporation is created. *Ohio & M. R. Co. v. McCarthy, 96 U. S. at page 258, 24 L. ed. p. 695; Union Pac. R. Co. v. Chicago, R. I. & P. R. Co., 163 U. S. 564, 41 L. ed. 265.* Moreover, the pledge agreement being on its face valid, the receiver, who asserts that it was *ultra vires*, had the burden of proving its invalidity, *Clews v. Jamieson, 182 U. S. at page 490, 45 L. ed. p. 1197*, that is, that the thing the First National Bank did was not convenient or useful to it in carrying out its express power to receive deposits. But the receiver neither rebutted this presumption nor met this burden of proof; in fact he offered no evidence upon the trial of the case (R. 88).

As stated by Attorney General Gregory, "the power to receive deposits, expressly granted to every national bank * * * is indispensable to the conduct of banking, and the extent of its exercise is in a degree the measure of the success of the bank"[1]; and, as found by the Supreme Court of Tennessee in *Grigsby v. Peoples Bank, 158 Tenn. 193*, the practice of giving security for deposits "is a practice followed by many banks". Properly, therefore, it should be held that the means by which de-

1 Supra, pages 47-49.

posits are to be secured, not being limited or restricted by statute, should be left to the discretion of the bank's officers and directors who know best what is convenient or useful to it. Such holding is especially warranted by the facts of the case at bar which clearly bring it within the principle that "whatever may fairly be regarded as incidental to, or consequential upon those things which the Legislature has authorized, ought not, unless expressly prohibited, to be held, by judicial construction to be ultra vires". *Jacksonville, Mayport, Pablo R. & Nav. Co. v. Hooper, 160 U. S. 514, 523, 40 L. ed. p. 523.*

Fourth, Fifth and Sixth Propositions

4. The Receiver of The First National Bank of El Paso, Texas, has no power to question the validity of the pledge agreement.

Scott v. Armstrong, 146 U. S. 499, 510, 36 L. ed. 1059, 1063; Jones v. New York Guaranty & I. Co., 101 U. S. 622, 25 L. ed. 1030, 1035; Sioux City Terminal R. & Wareh. Co. v. Trust Co. of N. A., 173 U. S. 99, 110, 43 L. ed. 628, 632; Blair v. Chicago, 201 U. S. 400, 450, 50 L. ed. 801, 822; Case v. Terrell, 78 U. S. 199, 20 L. ed. 134; Thompson v. St. Nicholas National Bank, 146 U. S. 240, 36 L. ed. 956.

5. The receiver of a national bank is estopped from asserting the want of power in that bank, while solvent, to pledge as security for deposits a portion of its assets, equivalent in amount to those deposits, in lieu of corporate surety bonds, which the bank furnished at its expense to procure such deposits, when the substitution was made for the purpose of saving bond premiums and affording adequate security due to the threatened withdrawal of one of the surety companies for which a substitute surety company could not be obtained, and when deposits have been made on the faith of the pledge agreement.

Chicago, R. I. & P. Co. v. Howard, 74 U. S. 392, 19 L. ed. 117, 121; Zabriskie v. Cleveland, C. & C. R. Co., 64 U. S. 381, 16 L. ed. 488, 498.

6. The receiver of a national bank is estopped from asserting the want of power in that bank, while solvent, to pledge as security for deposits a portion of its assets, equivalent in amount to those deposits, after national bank examiners, who learned of the pledge agreement from the books of the bank a month before its failure, made no complaint of the transaction and by their silence permitted the depositor to make further substantial deposits in reliance upon the pledge agreement.

Brown v. Schleier, 118 Fed. 981, affirmed *194 U. S. 18, 48 L. ed. 857.*

Argument Under Fourth, Fifth and Sixth Propositions

The Honorable Circuit Court of Appeals held that the receiver may disaffirm the pledge agreement without returning or tendering to the railroad company its deposits made on the faith of that agreement. This holding apparently is on the theory that the receiver defends this action solely in his capacity as a trustee for creditors—not as a representative of the bank—and that as such trustee he has a greater right to or equity in the pledged liberty bonds than had the bank itself (R. 125).

The receiver's powers are enumerated in sections 191 and 192 of the National Bank Act. It is provided

in section 191 that the Comptroller, when satisfied of the insolvency of a national banking association, may appoint a receiver "who shall proceed to close up such association, and enforce the personal liability of the shareholders". In section 192 it is provided that the receiver,—

> "shall take possession of the books, records, and assets of every description of such association, collect all debts, dues, and claims belonging to it, and, upon the order of a court of record of competent jurisdiction, may sell or compound all bad or doubtful debts, and, on a like order, may sell all the real and personal property of such association, on such terms as the court shall direct; and may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders".

The powers thus granted are not broad enough to authorize the receiver to challenge the validity of the pledge agreement which was executed by the bank and the railway company for the bank's benefit while it was solvent, and in furtherance of the bank's express power to receive deposits. Even in the case of *ultra vires* contracts this Honorable Court has held that no one but the sovereign is permitted to assert that a corporation's contract is *ultra vires*, unless by statute such person is authorized so to do. *Jones v. New York Guaranty & I. Co., 101 U. S. 622, 25 L. ed. 1030, 1035; Sioux City Terminal R. & Wareh. Co. v. Trust Co. of N. A., 173 U. S. at page 110, 43 L. ed. 632; Thompson v. St. Nicholas*

National Bank, 146 U. S. at page 251, 36 L. ed. 961; Blair v. Chicago, 201 U. S. at page 451, 50 L. ed. 822. The statutory power to question the validity of the pledge agreement is lacking, and the receiver "does not in any sense represent the government". *Case v. Terrell, 78 U. S. 199, 20 L. ed. 134, 135.*

It may be contended that the receiver, as a representative of the bank, can question the validity of the pledge agreement, but if so, he must first return or tender to the railway company its deposits made in reliance upon that agreement, as the bank would be required to do.

But it will be urged that the receiver, as a representative of the bank's creditors, may disaffirm the pledge agreement. It should be remembered that the liberty bonds, at the bank's suggestion, were pledged in lieu of surety bonds (R. 89, 91) for the benefit of the bank (R. 90, 94), in the regular course of its business (R. 66) and while it was solvent and a going concern (R. 46, 89). The transaction took place on January 29, 1931, some seven months before the bank became insolvent, and a full record thereof since that date has been carried on the bank's books (R. 92). Moreover, the creditors now represented by the receiver are those whose deposits no doubt were made since the bonds were pledged. Under these circumstances it is difficult to understand how those creditors or their rep-

resentative, the receiver, acquired any special property interest in the pledged bonds superior to that of the bank itself, and especially so since the railway company thereafter deposited a total of $148,765.75 relying on the pledge agreement, of which sum more than $54,000 on deposit when the bank failed would be distributed by the receiver to those creditors upon delivery of the pledged bonds to the railway company. But the receiver acquired no greater right in the pledged bonds than the bank had. This is made clear by at least two decisions of this Honorable Court. In *Scott v. Armstrong, 146 U. S. at page 507, 36 L. ed. p. 1062*, Chief Justice Fuller, speaking for the Court, held:

> "The receiver took the assets of the Fidelity Bank as a mere trustee for creditors, and not for value and without notice and, in the absence of statute to the contrary, subject to all claims and defenses that might have been interposed as against the insolvent corporation before the liens of the United States and of the general creditors attached."

And again, in *Fourth Street National Bank v. Yardley, 165 U. S. at page 653, 41 L. ed. p. 863*, this Court stated:

> "The receiver took no greater rights in the property of the insolvent bank which came into his possession than that which the insolvent bank possessed."

This being true, the receiver could not disaffirm the pledge agreement without returning or tendering to the railway company the full amount of its deposits made on the faith of that agreement unless the bank could have done so. The real question, therefore, is: Could the First National Bank have disaffirmed the agreement without returning the deposits?

In answering this question affirmatively, the Circuit Court of Appeals relied upon *California Nat. Bank v. Kennedy, 167 U. S. 362, Union Pac. Ry. v. Chicago, 163 U. S. 564,* and *Central Transportation Co. v. Pullman Car Co., 139 U. S. 60* (R. 125). In those cases the Court was dealing with contracts which were, to use the language of Mr. Justice Gray in the Pullman Car case, "ultra vires in the proper sense, that is to say, outside the object of its (the corporation's) creation as defined in the law of its organization, and therefore beyond the powers conferred upon it by the legislature" (139 U. S. 59, 35 L. ed. 68). For example: In *Central Transportation Co. v. Pullman's Palace Car Co., 139 U. S. 24, 35 L. ed. p. 55,* the leading case, this Honorable Court was called upon to determine the validity of a 99-year lease and Mr. Justice Gray stated:

> "The plaintiff not only parts with all its means of carrying on the business, and of performing the duty, for which it had been chartered, * * * but it undertakes to transfer, for ninety-nine years,

> nearly co-extensive with the duration of its own corporate existence, the whole conduct of its business, and the performance of all its public duties, to another corporation * * *."
>
> "Considering the long term of the indenture, * * * the frank avowal in the indenture itself, of the intention of the two corporations to prevent competition and to create a monopoly, there can be no doubt that * * * the real purpose of the transactions was, under the guise of a lease of personal property, to transfer to the defendant nearly the whole corporate franchise of the plaintiff * * *" (U. S. pp. 52-53; L. ed. p. 66).

It is not surprising, therefore, that the Court in that case found: "The necessary conclusion from these premises is, that the contract sued on was unlawful and void, because it was beyond the powers conferred upon the plaintiff by the legislature * * *" (U. S. p. 53, L. ed. p. 66); or that plaintiff's plea of estoppel met with this positive denial by the Supreme Court:

> "It was argued in behalf of the plaintiff that, even if the contract sued on was void, because ultra vires and against public policy, yet that, having been fully performed on the part of the plaintiff, and the benefits of it received by the defendant, for the period covered by the declaration, the defendant was estopped to set up the invalidity of the contract as a defense to this action to recover the compensation agreed on for that period.

> "But this argument, though sustained by decisions in some of the states, finds no support in the judgments of this court" (U. S. pp. 54-55, L. ed. p. 67).

In *California Nat. Bank v. Kennedy, 167 U. S. 362, 42 L. ed. 198*, the Supreme Court was considering the power of the California National Bank to acquire 990 shares of stock of the California Savings Bank, and the resultant liability of the former as a shareholder of the latter which had become insolvent. The questions before the Court were thus stated by Mr. Justice White:

> "1st, Do the statutes of the United States (U. S. Rev. Stat. §5136 et seq.) relating to the organization and powers of national banks prohibit them from purchasing or subscribing to the stock of another corporation? And, 2nd, If a national bank does not possess such power, can the want of authority be urged by the bank to defeat an attempt to enforce against it the liability of a stockholder?" (U. S. p. 366, L. ed. p. 200).

After holding that "the United States statutes relative to national banks constitute the measure of the authority of such corporations, and that they cannot rightfully exercise any powers except those expressly granted or which are incidental to carrying on the business for which they are established" this Court found that "a national bank does not possess the power to deal in

stocks" because "the prohibition is implied from the failure to grant the power" (167 U. S. 366-367, 42 L. ed. 200). In this connection it should be noted that section 24 of the National Bank Act (12 U. S. C. A. Title 12, chap. 2) does not authorize the dealing in stocks, but limits national banks to the transaction of the business of banking "by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes * * *". Hence the Court's holding that the failure to grant the power was an implied prohibition against its exercise. The Court also observed:

> "On behalf of the plaintiff below it was admitted at the trial that the stock of the savings bank was not 'taken as security or anything of the kind', and it is not disputed in the argument at bar that the transaction by which this stock was placed in the name of the bank was one not in the course of the business of banking for which the bank was organized" (U. S. p. 367, L. ed. p. 200).

Having found that dealing in stock was "entirely outside of the powers conferred upon the bank, and was in nowise the transaction of banking business or incidental to the exercise of the powers conferred upon the bank" (U. S. p. 370, L. ed. p. 201), the Court concluded

that the California National Bank was not estopped, by accepting stock dividends, from asserting its want of authority to purchase the stock in defense of an action against it as a shareholder. But the Court expressly stated that these facts distinguished the case from such cases as *National Bank v. Whitney, 103 U. S. 99, 26 L. ed. 443*, and *Union National Bank v. Matthews, 96 U. S. 621, 25 L. ed. 188* (U. S. p. 370, 371, L. ed. p. 201).

In the Whitney case, the Court, basing its decision on the Matthews case, upheld the power of a national bank to accept real estate security for future advancements to the mortgagor, although the National Bank Act only authorized the loaning of money on personal security, and the holding of real estate as security for debts previously contracted. In the Matthews case, the Court upheld the power of a national bank to accept as security for a contemporaneous loan a mortgage upon real property, and held that the borrower could not defend an action for foreclosure, upon non-payment of his note, by asserting the bank's want of power to accept the mortgage security. In the latter case this was said:

> "As the transaction is disclosed in the record, the loan was made upon the note as well as the deed of trust. * * * The deed, as a mortgage would have been, was an incident to the note * * *.
>
> "The intent, not the letter of the statute, constitutes the law. A court of equity is always re-

luctant in the last degree to make a decree which will effect a forfeiture. The Bank parted with its money in good faith. Its garments are unspotted. Under these circumstances, the defense of ultra vires, if it can be made, does not address itself favorably to the mind of the Chancellor.".

* * * *

"The statute does not declare such a security void. It is silent upon the subject. If Congress so meant, it would have been easy to say so; and it is hardly to be believed that this would not have been done, instead of leaving the question to be settled by the uncertain result of litigation and judicial decision" (25 L. ed. 189).

* * * *

"Where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable, and the sovereign alone can object. It is valid until assailed in a direct proceeding instituted for that purpose."

* * * *

"Sedg. Stat. and Const. Constr., 73, says: 'Where it is a simple question of authority to contract, arising either on a question of regularity of organization or of power conferred by the charter, a party who has had the benefit of the agreement cannot be permitted in an action founded upon it to question its validity. It would be in the highest degree inequitable and unjust to permit a defendant to repudiate a contract, the benefit of which he retains' " (25 L. ed. 190).

In *Union P. R. Co. v. Chicago, R. I. & P. R. Co., 163 U. S. 564, 41 L. ed. 265*, this Honorable Court upheld the power of a railroad company to grant trackage rights to another railroad company in the City of St. Louis. The following pertinent statements are extracted from the Court's opinion:

> "The general rule is that a contract by which a railroad company renders itself incapable of performing its duties to the public or attempts to absolve itself from those obligations without the consent of the state, or a contract made by a corporation beyond the scope of its powers, express or implied, on a proper construction of its charter, cannot be enforced or rendered enforceable by the application of the doctrine of estoppel. Thomas v. West Jersey R. Co., 101 U. S. 71 (25:950); Central Transp. Co. v. Pullman's Palace Car Co., 139 U. S. 24 (35: 55).
>
> "But where the subject matter of the contract is not foreign to the purposes for which the corporation is created, a contract embracing 'whatever may fairly be regarded as incidental to, or consequential upon, those things which the legislature has authorized, ought not, unless expressly prohibited, to be held by judicial construction to be ultra vires'. Jacksonville, M. P. R. & Nav. Co. v. Hooper, 160 U. S. 514, 525 (40: 515, 523); Atty. Gen. v. Great Eastern R. Co., L. R. 5 App. Cas. 473, 478; Brown v. Winnisimmet Co., 11 Allen, 326, 334" (163 U. S. p. 581-82; 41 L. ed. 271).

* * * *

"We think that it would be carrying the doctrine of *ultra vires* much too far to deny absolutely the competency of a railroad company, being a public highway, whose use is common to all citizens, to contract to give another running rights over its tracks without express statutory authority; and that under proper circumstances such a contract may well be held within its implied powers" (163 U. S. p. 585; 41 L. ed. 273).

* * * *

"The leading cases of Thomas v. West Jersey R. Co., 101 U. S. 71. (25:950); Pennsylvania R. Co. v. St. Louis, A. & T. H. R. Co., 118 U. S. 290 (30: 83); Oregon R. & Nav. Co. v. Oregonian R. Co., 130 U. S. 1 (32:837); Central Transp. Co. v. Pullman Palace Car Co., 139 U. S. 24 (35:55); St. Louis, V. & T. H. R. Co. v. Terre Haute & I. R. Co., 145 U. S. 393 (36:748); United States v. Union P. R. Co., 160 U. S. 1 (40:319), arose upon instruments which dispossessed the corporations of all of their property and of all capacity to perform their public duties. But we have no such case here" (163 U. S. 590; 41 L. ed. 274).

* * * *

"We do not feel called upon to enter at length upon other objections urged by appellants' counsel. One of them was that the Rock Island and St. Paul companies derived no power from the laws of Nebraska to enter into the alleged contract because they had not complied with the statutes of the state in that behalf. * * * The Rock Island Company built its road from South Omaha to Lincoln as vested with the corporate power to do so, and it contracted as in the possession of the

power as a corporation existing in and under the laws of Nebraska. The state appears to have been content, and the contract, not being necessarily beyond the scope of the powers of the corporation, must, in the absence of proof to the contrary, be deemed valid" (163 U. S. 591-92; 41 L. ed. 275).

* * * *

"* * * Courts may be permitted, where there is no legislative prohibition shown, to put a favorable construction upon such exercise of power by railroad companies as is necessary to promote the success of the company within its chartered powers * * *" (163 U. S. 594; 41 L. ed. 276).

The two following cases should be added to those cited in the foregoing opinion:

Ohio & M. R. Co. v. McCarthy, 96 U. S. at page 258, 24 L. ed. p. 695:

"* * * When a contract is not on its face necessarily beyond the scope of the power of the corporation by which it was made, it will, in the absence of proof to the contrary, be presumed to be valid. Corporations are presumed to contract within their powers. The doctrine of ultra vires, when invoked for or against a corporation, should not be allowed to prevail where it would defeat the ends of justice or work a legal wrong * * *."

Chicago, R. I. & P. Co. v. Howard, 74 U. S. at page 392, 19 L. ed. p. 121:

"Corporations as much as individuals are bound to good faith and fair dealing, and the rule is well

settled that they cannot, by their acts, representations or silence, involve others in onerous engagements and then turn round and disavow their acts and defeat the just expectations which their own conduct has superinduced".

This Honorable Court will perceive the distinction between the Pullman Car and California National Bank cases, cited by the Circuit Court of Appeals, and the case at bar. As stated by this Court in *Union P. R. Co. v. Chicago, R. I. & P. R. Co.*, supra, the contract in the Pullman Car case "dispossessed the corporation of all of its property and of all capacity to perform its public duties (163 U. S. 590, 41 L. ed. 274). In the California case, the purchase of stock in the savings bank was "entirely outside of the powers conferred upon the bank, and was in nowise the transaction of banking business or incidental to the exercise of the powers conferred upon the bank" (167 U. S. 370, 42 L. ed. 201). In the case now before the Court the pledge was made in carrying out the power expressly conferred to do a banking business by receiving deposits. We do not find any case by this Honorable Court which holds that a party enjoying the benefits of this character of contract may escape his just responsibilities by a plea of ultra vires, or that such defense will not be rendered nugatory by the law of estoppel.

There is another cogent reason for holding that the receiver cannot disaffirm the pledge agreement without returning or tendering to the railway company the full amount of its deposits. National bank examiners acting under the supervision and control of the Comptroller of the Currency made an examination of the First National Bank commencing on August 6, 1931. A day or so later they learned from the bank's books that liberty bonds of the par value of $50,000 were pledged to secure the Texas and Pacific's deposits, but none of the bank's officers were notified or advised by either the bank examiners or the Comptroller that the pledge of bonds was either irregular, illegal or beyond the powers of the bank (R. 94-95). If the Comptroller and his agents, the bank examiners, thought the pledge of bonds an ultra vires act, certainly it was their duty at once to so advise the bank's officers and to require that other valid security be given the railway company and the pledge agreement cancelled. Had this been done, the Texas and Pacific's deposits could have been secured in a manner satisfactory to the Comptroller, or its deposits could have been withdrawn. Surely it cannot be that one agent of the Comptroller, the receiver, will be permitted to disaffirm an agreement which impliedly

has been sanctioned by other agents of the Comptroller, the bank examiners, after the other contracting party has acted upon that assurance to his detriment. This extract from the opinion in *Brown v. Schleier, 118 Fed. 981*, affirmed *194 U. S. 18, 48 L. ed. 857*, is pertinent:

> "We think that, in virtue of his office as receiver, he is not authorized to challenge or impeach an executed transaction between the bank and a third party, that was simply ultra vires, and which, though known to the United States, through its proper officials, at the time it was undertaken and consummated, was neither arrested nor complained of by the United States or any creditor or stockholder of the bank."

When the receiver took charge of the First National Bank the pledge agreement had been performed by all parties except the bank's trust officer who held the liberty bonds as a trustee for the railway company. The bank had made the pledge and the Texas and Pacific had made the deposits; nothing remained to be done except the delivery by the trustee to the railway company of the liberty bonds to which it has shown itself justly entitled.

Seventh and Eighth Propositions

7. When a solvent national bank induces a depositor to cancel and surrender corporate surety bonds protecting its deposits and to accept in lieu thereof other security which the bank is without authority to furnish, moneys thereafter deposited in reliance upon that security are received by the bank as special deposits which it holds in trust for the use and benefit of the depositor, and those deposits, or an equivalent sum of money, may be recovered in full from the bank or from its receiver into whose hands they passed upon the bank's failure.

8. When a solvent national bank induces a depositor to cancel and surrender corporate surety bonds protecting its deposits and to accept in lieu thereof other security which the bank is without authority to furnish, the courts will enforce an implied agreement on the part of the bank to return the moneys deposited with it in reliance upon the invalid security, and those deposits never become general assets of the bank which its subsequently appointed receiver may distribute ratably among the bank's unsecured creditors.

Scott v. Armstrong, 146 U. S. 499, 507, 510, 36 L. ed. 1062-1063; Central Transportation Co. v. Pullman Car Co., 139 U. S. 24, 60, 35 L. ed. 55, 69; Aldrich v. Chemical National Bank, 176 U. S. 618, 636, 44 L. ed

611, 618; Citizens' National Bank v. Appleton, 216 U. S. 196, 206, 54 L. ed. 443, 446.

Argument Under Seventh and Eighth Propositions

The Circuit Court of Appeals has held that this is not a suit for benefits received, but one "upon a contract, to enforce it" (R. 125).

The amended bill of complaint (R. 1-20) substantially sets forth the matters incorporated in the foregoing statement of facts and contains an alternative plea to the effect that the railway company is entitled to recover from the receiver, as for money had and received, the full amount of its deposits in the First National Bank when it failed on September 4, 1931, if it is held that the pledge agreement is unenforceable (R. 10), and an alternative prayer for that relief (R. 12). If this Honorable Court should be of the opinion that the amended bill states only a cause of action upon the pledge agreement and if the Court should hold that such agreement is ultra vires and void and may be disaffirmed by the receiver, then your petitioner respectfully asks that such action of the Court be without prejudice to another cause of action by petitioner against the receiver for money had and received or for the recovery of or compensation for the money with which petitioner parted on the faith of the pledge agreement. *Central Transportation Co. v. Pullman's Car Co., 139 U. S. 24, 60, 35 L. ed. 55, 60;*

Pullman's Palace Car Co. v. Central Transportation Co., 171 U. S. 138, 43 L. ed. 108.

This Honorable Court in many decisions has held that even though a contract of a corporation be illegal and void, yet, if the other party thereto has actually performed it, in order to do justice between the parties, the courts will imply an agreement on the part of the corporation to return that which it has received by reason of the unlawful contract. We quote from a few of the leading cases to illustrate the rule:

Central Transportation Co. v. Pullman's Car Co., 139 U. S. at page 60, 35 L. ed. p. 69:

> "A contract *ultra vires* being unlawful and void, not because it is in itself immoral, but because the corporation, by the law of its creation, is incapable of making it, the courts, while refusing to maintain any action upon the unlawful contract, have always striven to do justice between the parties, so far as could be done consistently with adherence to law, by permitting property or money, parted with on the faith of the unlawful contract, to be recovered back, or compensation to be made for it. In such case, however, the action is not maintained upon the unlawful contract, nor according to its terms, but on an implied contract of the defendant to return, or, failing to do that, to make compensation for, property or money which it has no right to retain".

Aldrich v. Chemical National Bank, 176 U. S. at page 636, 44 L. ed. p. 618:

> "Suppose a national bank, in violation of the act of Congress, takes as security for a loan made by it a deed of trust of real estate, and subsequently causes the property to be sold and the proceeds applied in payment of its claim against the borrower, a surplus being left in its hands, which it uses in its business or in the discharge of its obligations. If sued by the borrower for the amount of such surplus, could the bank successfully resist payment upon the ground that the statute forbade it to make a loan of money on real estate security? Common honesty requires this question to be answered in the negative".

Citizens' National Bank v. Appleton, 216 U. S. at page 206, 54 L. ed. p. 446. (after quoting from the Pullman Car case, first above cited):

> "We need not go farther. It is entirely clear that the judgment against the defendant bank * * * was consistent with sound legal principles and was intrinsically right, even if the guaranty in question was beyond the power of the guaranteeing bank, under the national banking statutes. Whatever may be said as to the written guaranty, now alleged to be illegal, the judgment can be supported as based wholly on the implied contract, which made it the duty of the Central National Bank, under the facts disclosed, to account to the Cooper Exchange Bank for the money obtained

from the latter in execution of the agreement made by the former with the borrower".

Although holding that this is not a suit for benefits (R. 125), the Circuit Court of Appeals in effect has held that the bank received no benefits which may be recovered. This it accomplished by finding and concluding that the contract of deposit contained two agreements, viz: "One that the bank should pay back to the railway upon demand the sums deposited with it as other general deposits were. * * * The other is an agreement for security" (R. 124), and by holding that the moneys deposited by the railway company in reliance upon the invalid pledge agreement became general deposits the title to which ipso facto passed to the bank (R. 124-125).

The relationship between banker and depositor is one voluntarily assumed and must rest upon some contract between the parties. *Ruling Case Law, Vol. 3, p. 518.* Therefore, "whether a deposit in a bank is general or special depends upon the contract resulting from the mutual understanding and intention of the parties at the time such deposit is made". *Northern Sugar Corporation v. Thompson (C. C. A. 8th Circuit), 13 Fed. (2d) at page 831.* This the Circuit Court of Appeals conceded (R. 125), but, citing as authority its opinion in *Fagan v. Whiddon, 57 Fed. (2d) 631,* the

Court held "an agreement definitely fixing the character of the deposit as general may not be disregarded because, if the depositor had fully known the law and the facts, he would have acted differently for his protection" (R. 125). In that case the executors of Whiddon sought to impress certain funds in the hands of Fagan, receiver of the First National Bank of Avon Park, Florida, with a trust to the extent of Whiddon's savings deposits in that bank. After making the deposits, which the Court stated created the relationship of debtor and creditor, Whiddon was adjudged insane and his guardians, later his executors, "undertook to ascertain the nature and condition of the accounts and business of their award with the bank, the deposits that he had there and the property they held for him, and made general and specific inquiries of the officers of the bank; they sought and obtained an inventory and specifically inquired whether Whiddon had a savings account" (p. 631). The inventory furnished showed no savings account, and "the officer to whom the inquiry was referred, having full knowledge that his statement was false, advised that Whiddon had no savings account" (p. 631). After Whiddon's death, his executors relied upon the statements and representations of the bank's officer that Whiddon carried no savings account in the bank, and they did not ascertain that he had one until the bank had been placed in the

hands of a receiver. Had they known of the existence of the savings account, Whiddon's executors would have withdrawn the money before the bank failed (p. 631). After finding these facts the master, to whom the case was referred, concluded that,—

> "since the result of the fraudulent acts and concealments of the bank and its officers, if given effect to, would be in effect to permit the bank to tender a now insolvent for a then solvent debtor, and thus defraud appellees of the moneys they would then have received, the matter must be looked on as though the deposit had in fact been withdrawn, the relation of debtor and creditor terminated, and a new relation of trustee for a special fund created" (pp. 631-632).

The judgment of the District Court, adopting the master's conclusions of law, was reversed by the Circuit Court of Appeals, with directions to dismiss the bill. In support of its decision, the latter Court stated:

> "All that has occurred here is that a debtor bank has put off payment of its debt until it has become unable to pay it, by falsely stating to the representatives of the depositor that the debt did not exist. False and reprehensible though this conduct was, and liable as its authors undoubtedly are for the damage which it caused, its factual and legal character and consequences cannot, be-

> cause insolvency has ensued, by any kind of equitable intendment be converted from the false statement that the debt did not exist, into the true statement that it did, and an agreement that it would be regarded as withdrawn as a general and redeposited as a special deposit to be held by the bank not as its own money, for the amount of which it stands debtor to the depositor, but as the depositor's money of which it is trustee" (p. 632).

In the Whiddon case, the character of the deposits when made was definitely fixed as general, about which no controversy arose, and the novation in law which the executors sought to establish arose out of circumstances occuring after the deposits were made. In the case at bar the character of the deposits depends upon an agreement antedating or contemporaneous with the deposits by which the Texas and Pacific agreed that they might be general provided they were secured. This is made clear by the District Court's findings of fact that the president of the railway company informed the bank's vice president-cashier "that under no circumstances would The Texas and Pacific Railway Company continue its account with and deposits in the First National Bank of El Paso without full and adequate security" (R. 90), and that the railway company, believing the representations of the bank's officers and attorneys that the pledge agreement and liberty bonds "would protect the deposits of The Texas and Pacific Railway Company in The First

National Bank of El Paso as fully and to the same extent as said corporate bonds", accepted the pledge agreement and those bonds, cancelled the surety bonds and thereafter continued its account with and made deposits in the First National Bank "relying upon said pledge agreement and liberty bonds as security for its deposits" (R. 92-93). To hold otherwise would mean that the railway company agreed to place its moneys in the First National Bank as general deposits even though the pledge agreement was invalid. Such is contrary to the record in this case.

In support of its position that the Texas and Pacific placed its moneys on general deposit, the Circuit Court of Appeals declared that the railway company "was as fully charged with knowledge as the bank was" of the latter's "want of power" to make the contract for security (R. 125). This conclusion, of course, is predicated upon the Court's prior finding that national banks can only exercise those implied powers which are "necessary (that is, indispensable) to the proper conduct of the business of a national bank" (R. 124). This, as we have shown in the preceding section of this brief, is not the proper measure of the implied powers of national banks. Those banks are expressly authorized to exercise all such incidental powers as shall be necessary—that is, convenient or useful[1]—to

1 McCullough v. Maryland, supra, pages 42-44.

carry on the business of the bank, and what may be convenient or useful to it is purely a fact question peculiarly within the knowledge of the bank's officers. Moreover, "the mutual understanding and intention of the parties," *Northern Sugar Corporation v. Thompson*, supra, not the legal knowledge of the depositor, determines the character of the deposit, and since the Texas and Pacific required the bank to furnish corporate surety bonds for more than eight years and made it plain to the bank's officers when the pledge agreement was made that the railway company's account would be closed and its deposits withdrawn if they were not fully secured, it cannot be successfully contended that it was the mutual understanding and intention of the bank and the railway company that the title to the latter's deposits should vest in the bank if in fact the pledge agreement was void.

After January 29, 1931, when the liberty bonds were substituted for the surety bonds as security for its deposits, The Texas and Pacific Railway Company continued its account with and thereafter deposited in the First National Bank a total of $148,765.75 (R. 93), and at all times between January 29, 1931 and September 4, 1931, when the bank failed, the Texas and Pacific had an amount in excess of $50,000 on deposit (R. 47, 67, 81). At the close of the bank's business on August 6, 1931, the railway company had a balance of

$50,428.10, and it deposited an additional $16,545.48 between August 6 and September 3, 1931 (R. 84, 93). On the latter date the T as and Pacific had $54,325.90 in the bank to which sum was added a small interest payment and an unpaid cashier's check, thus raising the total to $54,646.94 as of September 4, 1931 (R. 84-85, 93). All of those funds were deposited subsequent to January 29, 1931, the date on which the liberty bonds were substituted as security for the Texas and Pacific's deposits (R. 93), and the so-called "assets" of which the receiver took charge on September 8, 1931 (R. 48) included those funds.

It is true that the receiver is directed by section 192 of the National Bank Act to take charge of all the bank's "assets" etc. and to pay over to the Treasurer of the United States, subject to the order of the Comptroller, all moneys received from the collection of debts, claims, and the sale of property, and the Comptroller by section 194 is directed to make a "ratable dividend" from time to time, under certain conditions, of the moneys turned over to him by the receiver, but this Honorable Court has held that "the requirement as to ratable dividends, is to make them from what belongs to the bank, and that which at the time of the insolvency belongs of right to the debtor does not belong to the bank" *Scott v. Armstrong, 146 U. S. at page 510, 36 L. ed. p. 1063.*

There is another aspect of this case which should not be overlooked. It is of record that the bank's vice president-cashier, who succeeded in getting the railway company to accept the pledge agreement and the liberty bonds in lieu of the corporate surety bonds, knew at the time he came to Dallas for that purpose that the Maryland Casualty Company, surety on one of the $25,000 bonds, intended to "get off" all bonds of the First National Bank; that the bank was "going to have to give up this Maryland Casualty bond"; that the railway company was being asked to accept the liberty bonds in lieu of the surety bonds partly because the bank knew that the Maryland Casualty Company would ask that the bond be canceled, or would not renew it; and that it was doubtful whether or not the bank could get a substitute standard surety company. But that bank official "did not mention" to the railway company's president "at the time this substitution was made, nor at any time thereafter, this substitution was desired on account of the surety company threatening to cancel its bonds. He never heard of that, so far as I know" (R. 63, 70-72). Had a full disclosure been made, the railway company would not have agreed to the cancellation of its surety bonds. Having obtained the railway company's deposits under these circumstances, which give rise to a constructive fraud, the Court should hold that the bank received them

as special deposits the title to which remained and now is in the railway company.

Since the First National Bank, if the pledge agreement be void, received the Texas and Pacific's deposits not as general but as special deposits, they never became the property of the bank which the receiver might distribute ratably to unsecured creditors, but the receiver took them as a part of the funds passing into his hands impressed with a trust in favor of the railway company.

Conclusion

As stated by Attorney General Gregory, "the power to receive deposits, expressly granted to every national bank * * * is, of course, indispensable to the conduct of banking, and the extent of its exercise is in a degree the measure of the success of the bank"; "the means by which depositors are to be protected and secured are not expressly limited or restricted by statute"; "a large discretion is left to the (bank's) officers and directors"; and "they may use such means for the purpose as are not prohibited by, or inconsistent with the provisions of, the law, and as they may reasonably find to be suitable and proper and not inconsistent with the prudent conduct of the affairs of the bank within the scope of its charter"[1]. That officers and directors of banks have availed themselves of this privilege is shown by the finding of the Supreme Court of Tennessee that the practice of giving security for deposits "is a practice followed by many banks", *Grigsby v. Peoples Bank, 158 Tenn. 193.*

The officers and directors of The First National Bank of El Paso, Texas, considered the exercise of that prerogative beneficial to the bank as shown by this record: Although admittedly solvent (R. 89), it became necessary for the First National to curtail expenses, including the premiums which it had been paying on the

1 Supra, pages 47-49.

surety bonds protecting the railway company's deposits (R. 64). In addition the Maryland Casualty Company, surety on one of those $25,000 bonds, had informed the officers of the bank that it was "going off" all bonds, and it was apparent the bank would experience difficulty in procuring a substitute surety company (R. 70-72). The bank's officers knew that the railway company with the cancellation of its bonds would close its account and withdraw its deposits (R. 90), and this they wished to avoid. They proffered to the Texas and Pacific a pledge of liberty bonds in lieu of the corporate surety bonds (R. 89), and, being unaware of the action of the Maryland Casualty Company the railway company, solely for the purpose of aiding the bank (R. 90), accepted the pledged liberty bonds, caused the surety bonds to be cancelled (R. 92-93), continued its account with the First National and thereafter deposited with it a total of $148,765.75 (R. 93).

This being true, we confidently believe this Honorable Court will find and hold (1) that the pledge of liberty bonds in lieu of the surety bonds as security for the railway company's deposits was a valid exercise by the First National Bank of a power incidental to its express power to receive deposits, (2) that the receiver may not disaffirm such pledge agreement, at least without returning or tendering to the Texas and

Pacific the full amount of its deposits made in reliance upon that agreement, and (3), in the alternative, that the railway company may recover from the receiver, as for money had and received which he holds in trust, the full amount of its deposits when the bank failed on September 4, 1931.

Wherefore, petitioner respectfully prays that this Honorable Court reverse the decree and judgment of the District Court and the Honorable Circuit Court of Appeals for the Fifth Circuit and remand this cause with direction to grant the relief sought by petitioner, that costs be taxed against respondent, and that such other orders and decrees be entered as to this Honorable Court petitioner may seem entitled in the premises.

Dated at Dallas, Texas, November 20, 1933.

Respectfully submitted,

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No. 128

CURRENCY BUREAU.

CERTIFICATION OF CHECKS ON NATIONAL BANK—ISSUE OF CASHIER'S CHECKS.

Office of the Comptroller of the Currency,

Washington, June 5, 1867.

DEAR SIR:—I notice by Mr. Callender's report of his examination of your Bank two points to which I desire to call your attention. I refer to the certification of broker's checks in excess of actual balances, and to the issue of cashiers' checks. The first I presume to be an abuse of a practice which has grown to be a necessity in the transaction of business in New York. Probably you would reject without hesitation a proposition to certify in this way for your depositors without discrimination, and very few outside of a particular class would have the imprudence to demand the privilege of overdrawing their accounts. How it happens that brokers alone claim this extraordinary indulgence, I am not prepared to explain. Why they cannot trust each other instead of requiring each other to put forward his bank as the responsible party in all transactions, I will leave you to explain. It only seems to me that the demand is utterly unreasonable and one that the banks would not only be justified in rejecting, but one that prudence would require them to repudiate. I do not say this as bearing particularly upon your particular case, but upon the practice in general; and I am much gratified to learn from Mr. Callender that you have expressed a readiness to lend your co-operation to some practicable remedy.

As to the second point, I ground my objection to the issue of cashiers' checks upon the law. A National Bank can borrow money in either of three different ways—by issuing bills of exchange, by receiving de-

posits, and by the issue of circulating notes. I find no other method authorized in section eight of the law which defines your corporate privileges. If a cashier's check is issued in payment of a depositor's check, it is paid out in lieu of the money called for by the depositor, and as such would be prohibited by the last clause of section twenty-three.

If the depositor has the money to his credit, he is entitled to receive it; if he has not, you are under no obligation to pay the check at all. In a personal interview with you I could talk of these things in a way that would not be objectionable; in a letter there is necessarily more of formality, and what I say may seem more dictatorial. I only wish you to understand that my only desire and study is how best to promote the interest entrusted to my charge, and I am confident that with the assistance and co-operation of the New York banks the national banking system can be made all that its most ardent friends could desire. But the New York bankers must take the lead—must give tone and hearty support. It rests with them to direct, control and perfect the system. If they would realize how much depends upon them, I should have no fears for the future.

Very respectfully,

H. R. HURLBURD,
Comptroller.

HON. E. HAIGHT,
President National Bank of the Commonwealth,
New York City.

The Internal Revenue Record.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1933.

No. 128.

THE TEXAS AND PACIFIC RAILWAY COMPANY, *Petitioner*,

versus

S. O. POTTORFF, RECEIVER OF THE FIRST NATIONAL BANK OF EL PASO, TEXAS, *Respondent*.

REPLY BRIEF OF THE TEXAS AND PACIFIC RAILWAY COMPANY.

To the Honorable the Supreme Court of the United States:

In the introductory statement of respondent's reply brief (page 3) an erroneous premise is assumed, namely: "It is settled that the provisions of this act as to discounting notes, receiving deposits, etc., are to be read as descriptive of the kind of banking which is authorized and as illustrative of incidental powers. * * * It follows that the incidental powers granted by the act are not those incidental to receiving deposits, etc., but are those 'necessary to carry on the business of banking' ".

If the provisions of the Act (section 24, par. 7) are "descriptive of the kind of banking which is authorized", obviously those provisions are not merely "illustrative of (the) incidental powers" granted. The conclusion, therefore, that "the incidental powers granted by the Act are not those incidental to receiving deposits" is clearly erroneous. Moreover, the cases cited by respondent hold that both the banking businesses specified in section 24 and the incidental powers necessary to carry on those businesses are granted.

In the second department of his reply brief, respondent states: "In determining what powers are 'necessary to carry on the business of banking,' we may well adopt as a general statement the definition of Mr. Chief Justice Marshall when he said that, necessary, 'imports no more than that one thing is convenient, or useful, or essential to another'." (page 4.) But respondent says Chief Justice Marshall's definition of the word "necessary" is tempered by Mr. Chief Justice Waite's statement in *First National Bank of Charlotte v. National Exchange Bank,* that a national bank's incidental powers "are such as are required to meet all the legitimate demands of the authorized business, and to enable the bank to conduct its affairs within the general scope of its charter, safely and prudently (92 U. S. p. 122, 23 L. ed. pp. 679-681). From this premise it is argued, not that the particular pledge in the case at bar was unsafe or imprudent, but that as a general proposition it would neither be safe nor prudent for national banks to possess and exercise the implied power to pledge assets to secure deposits. This, of course, is simply another way of saying that such pledges are against public policy. This

theory of the case was urged in, but was rejected by, the Honorable Circuit Court of Appeals.

The court below did not state its reasons for rejecting respondent's contentions that the pledge was against public policy, but it may have shared the views of the Supreme Court of Indiana on the subject. That Court said in *Schornick v. Butler, 185 N. E. 111, 112-113:*

> "It is urged that it is against public policy to permit banks to pledge assets to secure the payment of deposits.
>
> "Constitutional and statutory enactments, practices of officials, and judicial decisions may be looked to for a disclosure of the public policy of a state. Legislative enactments are the safest guides and the fairest in that they operate prospectively and as a guide to future negotiations. Decisions of courts of last resort operate in the same manner after their pronouncement, but in the first instance may have the effect of destroying the contract made before the public policy is announced.
>
> "'Without minimizing the importance of the doctrine that contracts should not be enforced if they contravene public policy, many courts have cautioned against recklessness in condemning contracts as being in violation of public policy. Public policy, some courts have said, is a term of vague and uncertain meaning, which it pertains to the lawmaking power to define, and courts are apt to encroach upon the domain of that branch of the government if they characterize a transaction as invalid because it is contrary to public policy, unless the transaction contravenes some postive statute or some well-established rule of law. Other courts have approached the remark of an English judge that public policy is an unruly horse astride of which one may be carried into unknown paths. Considerations such as these have led to the statement that the power of the

courts to declare a contract void for being in contravention of sound public policy is a very delicate and undefined power, and, like the power to declare a statute unconstitutional, should be exercised only in cases free from doubt.' Hogston v. Bell, 185 Ind. 536, at page 544, 112 N. E. 883, 885."

Or, the Circuit Court of Appeals may have approved the reasoning of Judge Dickinson who dissented in *Baltimore & O. R. Co. v. Smith*, wherein he stated in part:

"The policy of the law: This takes us into the domain of economics, a subject the limits of which are expansive and elastic. The practice said to be condemned as against the policy of the law is that of securing depositors. The first query aroused is how any act or practice can be one which the law condemns when it is the very act or practice which the law enjoins. The banking policy or practice of securing deposits may be wise or foolish, sound or unsound, good or bad. There may or may not be room for a difference of opinion on the subject, but the policy or practice is the same whether the deposit secured is that of A or B. How can A insist that the bank secure his deposit and yet condemn the bank for doing something against the policy of the law if the deposit of B is likewise made secure? Does it change the situation any if A is an official or the moneys deposited by him are public moneys? We are not speaking of the power or wisdom of the Legislature in laying down one rule of policy for public deposits and another for private but of the wholly different question of whether the courts should condemn as against the policy of the law something which the law enjoins when its own interests are affected. It is easy to understand that any banking practice may in the judgment of the members of a court be condemned as unwise or even ruinous in its consequences,

but can it for this reason be found to be illegal because against the policy of the law? * * * With respect to banking policies the managers of no bank have the wish to harm it, and any policy which is followed by the banks is quite as likely to be sound if left to the judgment of trained bankers as it is if dictated by the courts following any supposed policy of the law." (56 Fed. (2d) 799, 804, 805.)

Respondent lays much stress upon *Thomas v. West Jersey Railroad Company, 101 U. S. 71, 25 L. ed. 950,* but the particular contract in that case rendered the carrier unable to perform its public functions because by it the company's "railroad and all appurtenances and franchises, including the right to do the business of a railroad" were surrendered to another company (U. S. p. 79, L. ed. p. 951). We have no such condition here.

Although offering no evidence upon the trial of this case (R. 88), respondent now advances numerous arguments to prove that, generally speaking, the pledging of assets to secure "private" deposits "is calculated to render a bank unsafe and incapable of performing its proper functions" and "is destructive of sound banking, is not useful or essential, is not necessary, and is therefore not within the authority conferred by implication" (page 5).

Let us examine these arguments, in the order presented.

Prefacing his remarks the respondent observes that "national banks have become charged with a public interest" (page 6), but so has the railway company who stands to lose the greater portion of its deposit if the judgments of the lower courts are upheld.

The receiver states, "It is a far cry from the private banker of old England to the modern institution of today"

(page 6). In some respects this may be true, but the deposit system of today is similar to the first banking business in England. We quote from the opinion of this Honorable Court in *Auten v. United States National Bank of New York, 174 U. S. at page 142, 43 L. ed. p. 926:*

> "The very first banking in England was pure borrowing. It consisted in receiving money in exchange for which promissory notes were given payable to bearer on demand, and so essentially was this banking as then understood, that the monopoly given to the Bank of England was secured by prohibiting any partnership of more than six persons 'to borrow, owe or take up any sum or sums of money on their bills or notes payable at demand.' And it had effect until 1772 (about thirty years), when the monopoly was evaded by the introduction of the deposit system. The relations created are the same as those created by the issue of notes. In both a debt is created—the evidence only is different. In one case it is a credit on the banker's books; in the other his written promise to pay. In the one case he discharges it by paying the orders (cheques) of his creditor; in the other by redeeming his promises. These are the only differences. There may be others of advantage and ultimate effect, but with them we are not concerned."

It is stated that "banks in these days must publish at stated intervals reports which show the nature of their assets and liabilities" (page 6). Respondent apparently refers to section 161 of the National Bank Act, as amended Feb. 25, 1927, c. 191, § 13, 44 Stat. 1232, which reads in part:

> "Every association shall make to the Comptroller of the Currency not less than three reports during each year, according to form which may be prescribed by

him * * *. Each such report shall exhibit, in detail and under appropriate heads, the resources and liabilities of the association at the close of business on any past day by him specified, and shall be transmitted to the comptroller within five days after the receipt of a request or requisition therefor from him; and the statement of resources and liabilities, together with acknowledgment and attestation in the same form in which it is made to the comptroller, shall be published in a newspaper published in the place where such association is established * * *. The comptroller shall also have power to call for special reports from any particular association whenever in his judgment the same are necessary in order to obtain a full and complete knowledge of its condition."

In connection with the reports of national banks to the Comptroller, and to the public, respondent says:

> "As they are now prepared, these reports make no mention of pledges which may have been made to secure individual private deposits. The public is led to believe that all of the particular bank's assets, except such as may, in accordance with law, secure public deposits, stand as security for the payment of all private deposits, without preference, and upon the strictest equality. If present publications are continued and pledges are made to secure private deposits, such pledges will be made in secret so far as the public is concerned. The result is the perpetration of the grossest fraud on unsecured creditors of the bank" (page 6).

The form of report required by the Comptroller is not of record, and presumably respondent wishes the Court to take judicial notice of its provisions. Should this be done the Court will find that such reports did not inform either the

Comptroller or the public of assets pledged to secure public deposits. Furthermore, the Comptroller has the power to compel national banks to make a full disclosure to the public of all pledges, both public and private, for section 161 requires that reports to the public and to the Comptroller be prepared "according to the form which may be prescribed by him".

We note these statements by Circuit Judge Alschuler in his dissenting opinion in *Sneeden v. City of Marion, Ill., 64 Fed. (2d) 721, 731:*

> "It is pointed out * * * that ordinarily there is secrecy in such (public) pledges of which the general public has no notice, and that depositors not so secured would usually have no means of knowing how much of the bank's reported assets are so segregated.
>
> "It seems to me that the vice is not with the pledging of the assets, but with the laws and regulations concerning reports and advertisements of banks."

The receiver asserts that banks should not have the implied power to pledge assets to secure deposits, because in some instances the value of the pledged securities might greatly exceed the amount of the deposit (pages 7-8). In the case at bar the railway company maintained an average daily deposit in the bank in excess of $50,000, the par value of the pledged liberty bonds (R. 46, 47, 93). Furthermore, it is extremely doubtful that any banker could ever be coaxed into giving more than a dollar security for a dollar deposit.

Respondent fears that the pledging of assets to secure deposits might lead to some creditors being preferred over others in the event of insolvency. All pledges made after the commission of an act of insolvency or in contemplation

thereof, are declared void by section 91 of the National Bank Act, but "liens, equities or rights arising * * * prior to insolvency and not in contemplation thereof are not invalidated". "The provisions of the Act are not directed against all liens, securities, pledges or equities, whereby one creditor may obtain a greater payment than another, but against those given or arising after or in contemplation of insolvency". *Scott v. Armstrong, 146 U. S. at page 510, 36 L. Ed. page 1063.*

Respondent contends (page 9) that the absence of any case in the Federal Courts prior to 1931 involving a pledge of assets to secure a private deposit is evidence that the practice has not been found necessary or helpful, but he asserts that the absence in those Courts for a long period of any case involving a pledge of assets to secure a public deposit is explained by the Comptroller's recognition of the validity of such pledges. Might not the absence of litigations over private deposits be likewise explained?

We note this statement in Judge Dickinson's dissenting opinion in *Baltimore & O. R. Co. v. Smith, 56 Fed. (2d) 799, 804:*

> "The practice has of late grown up, and recent happenings in banking circles has doubtless furthered it for depositors, particularly those carrying large balances such as railroads, trustees for estates, and banking institutions to ask for and receive security for their deposits. Comptrollers have known of this. Some of them have doubtless scolded; but they have permitted it * * *."

We find nothing in the record to support respondent's statement that the pledge "did not take place until the heavy withdrawals, which closed the bank, had begun"

(page 10). However, the existence of such condition would have warranted the officers of the bank in making the pledge to prevent the withdrawal of the railway company's deposits when the surety company went off the bank's bond protecting those deposits.

The receiver says "if each depositor insists upon his deposit being guaranteed by the pledge of collateral, the bank's ability to lend, and thereby earn a profit, is seriously impaired" (page 10). This is obviously untrue because for each dollar of security pledged the bank receives a dollar by deposit which it may in turn lend to others.

Respondent also argues that securing deposits is a bad banking policy. A similar argument was rejected by the Supreme Court of Indiana in *Schornick v. Butler, supra.* The Court said:

> "It is urged that it is bad policy for banks to give security for money deposited. That unless security is given for all deposits, unsecured depositors will withdraw their funds and thus destroy the business of the bank. This is a question of business policy with which we are not concerned, but it is well known that banks do pay interest on some types of deposit and not in others." (185 N. E. 112.)

It is contended that the pledging of assets to secure some depositors, will drive other depositors away and thus bring ruin upon the banks, disabling them from performing their public functions. This has not proved true in the cases of security for public deposits, and in those cases the individual depositor has the same reasons to complain.

Banks depend in a large measure upon the accounts of large depositors who require security. If national banks

cannot give that security, it may be expected that those accounts will go elsewhere, to state or private bankers, with resulting injury to the losing banks. Judge Dickinson considered this in his dissent in the Smith case. He stated:

> "A word should be added on behalf of the depositor. He may be the trustee of an estate holding moneys for which he and his sureties are responsible. Why should he be denied a protection which is granted to the custodian of public moneys? Surely neither the bank nor other depositors are harmed and may be benefited. Assume the case of such a trustee with a large deposit balance. He may have no need to withdraw his moneys but he may be alarmed. If secured, he will leave his moneys with the bank. If not secured, what may he do and with what consequences to the bank, to its stockholders, and its other depositors?" (56 Fed. (2d) 799, 805.)

The receiver states that the Comptroller has consistently maintained the position that National banks have no power to pledge assets to secure private deposits (page 11). Although no evidence was introduced by the receiver upon the trial of this case he now seeks to support this statement by appending to his reply brief copies of two letters written by Deputy Comptroller F. G. Awalt: one dated December 13, 1929, addressed to a Grand Secretary of the Grand Lodge A. F. & A. M. of Nebraska, at Omaha; and the other dated January 30, 1931, and addressed to the President of the First National Bank of Hornell, New York. These letters, of course, are improperly before the Court; furthermore, they do not support the receiver's contention, one being addressed to a fraternal association and the other written the day *after* the pledge agreement was made in

the case at bar. If this be a departmental interpretation by the Comptroller, which is denied, it certainly cannot be given retroactive effect. *Shearer v. Anderson, 16 Fed. (2d), 995, 996.*

Respondent quotes from *Baltimore & O. R. Co. v. Smith, 56 Fed. (2d) 799,* in which the Court states that "it is admitted that whenever the Comptroller was asked for an opinion as to the power of national banks to pledge collateral to secure private deposits, in every instance, he has disapproved of such pledges and held that, in his opinion, national banks do not have that power." It is clear that the receiver cannot, after the record is closed, make proof in this case by referring to a different case in which the judgment was based upon an agreed statement of facts.

The letter of the acting Secretary of the Treasury addressed to the House Committee in charge of Senate Bill 486, and set out on pages 12 and 13 of respondent's reply brief, relates wholly to the securing of public monies of States and their political subdivisions, and does not indicate the attitude of the Secretary towards the pledging of assets to secure private deposits.

Certain testimony given by respondent is set out on page 14 of his reply brief, followed by this statement:

> "It is thus apparent that neither the Comptroller nor any of his examiners knew of this pledge until shortly before the bank was closed, and that the Comptroller was never called upon to pass on the validity of this pledge."

Respondent failed to quote this testimony given by the receiver:

> "I could not tell the date the examiners made examination of the securities of this railway; very likely

was the first day the examination started, because the first thing the examiners do when they come is verify the cash and check up the securities" (R. 83).

Furthermore, the trial court found that,—

"National Bank Examiners, acting under the supervision and control of the Comptroller of the Currency made an examination of The First National Bank of El Paso, commencing at 8 o'clock A. M. on August 6, 1931, and ending at noon on August 20, 1931. The report of said bank examiners to the Comptroller covering the condition of said bank showed that liberty bonds of the par value of $50,000:00, were then pledged to secure the deposit of The Texas and Pacific Railway Company. This information was obtained from the books of the bank probably during the first two or three days of the examination."

The bank examiners were agents of the Comptroller and information obtained by them was imputed to the Comptroller.

The receiver contends that "Congress, by passing the Act of June 25, 1930, section 45 (R. S. 5153), made it clear that national banks should thereafter have no power to pledge their assets to secure private deposits" (page 15). This argument was urged in the Circuit Court of Appeals without success. It will be noted that the opinion of that Court is not at all predicated upon this theory. Furthermore, the legislative history of that Act, as set forth in *Baltimore & O. R. Co. v. Smith, 56 Fed. (2d) 799, 802,* disproves this contention.

Senate Bill 486, 71st Congress, 2d session, which became the Act of June 25, 1930, was designed to remove certain doubts in the mind of the Attorney General for the State of

Minnesota as to the power of national banks to pledge their assets as security for the deposits of that State and its political subdivisions. The report of the Senate committee was based upon a letter from the Attorney General of Minnesota in which he thus voiced his anxiety:

> "* * * The national banks of this State have pledged with the State and the various subdivisions thereof millions of dollars in Government and other bonds as security for public deposits. They are anxious to be permitted to do so, and we are willing that they should. Under the law as it now stands we may be taking a chance in accepting such pledges from the national banks, and we should like to have the chance removed by legislation in Congress which will *specifically* authorize such pledges by national banks" (our italic).

And the House committee reported S. 486 favorably because of a request from the Acting Secretary of the Treasury, reading in part as follows:

> "'While the office of the Comptroller of the Currency has consistently taken the position that national banks have the right to give security for the safekeeping and prompt payment of public moneys of the State or political subdivision thereof deposited with such national banking associations, several recent decisions have thrown some doubt on this question with the result that in some States the State banks may secure the public deposits, but the officers of the State are in doubt about depositing with the national banks in the absence of any *specific* law by Congress on the subject. It would be extremely helpful, therefore, if it is possible for your committee to report out, and the House pass, S. 486'" (our italic).

It thus clearly appears that Congress, by amending section 90 of the National Bank Act to afford the specific relief sought, had no intention to and in fact did not amend or restrict any power granted to national banks by section 24 of that Act, and did not declare that "national banks should thereafter have no power to pledge their assets to secure private deposits".

In response to the statements of Mr. Bernard F. Cataldo concerning the distinction between loans and deposits, and the opinions on that subject of the courts of Minnesota and North Dakota (respondent's reply brief, page 19-21), we respectfully refer again to the opinion of this Honorable Court holding that a deposit is a loan[1], and extract the following from the opinion of the Supreme Court of Indiana (March 28, 1933), in the case of *Schornick v. Butler, 185 N. E. 111, 112:*

> "The right of a bank to borrow money and pledge its assets for the payment thereof is beyond serious question. It is urged, however, that a deposit is not a loan and that banks have no power to pledge their assets to secure deposits. There is no reason for the distinction. In either case the relation of debtor and creditor is created. * * * Generally a loan differs from the ordinary deposit only in the evidence of the promise, the time of payment, and the interest rate. The relation created is the same. It is a well-recognized fact that banks in some instances pay various rates of interest upon ordinary checking accounts as well as upon time deposits against which certificates are issued, payable on demand after a certain date, and that they also on occasion borrow money at varying interest rates upon their promissory notes payable upon a date cer-

[1] Petitioner's original brief, p. 39.

> tain. The basic contractual obligation to pay is the same and, if when the money is received the bank assigns collateral as a guaranty of its repayment, we know of no rule or reason which would permit the collateral to be retained in one case and not in another".

It is here noted that Mr. Cataldo's remarks appear in that section of his writings in which public deposits are discussed and that he admits, on the last page of his paper, that if the Courts uphold the analogy between a deposit and a loan, no distinction exists between a public and a private deposit.

Respondent relies upon Mr. Cataldo (pages 22-23) to prove that a bank's creditors are injured when it, while solvent, pledges assets to secure deposits. Again the author's remarks concern public deposits.

In reply, we quote the Supreme Court of Indiana in *Schornick v. Butler, supra:*

> "The municipality to whom the bond was given was not a creditor of the bank nor would it have become a creditor unless the bond was given.
>
> No question of preferring creditors is involved. * * * The bank parted with an interest in the securities equal to the deposit subject to the condition that, to the extent to which it repaid the cash, it would reclaim the securities. It amounts to no more than a sale of securities at their actual value for cash. The general depositors of the bank lost nothing by the transaction, and, if they are affected at all, they are benefited since the bank is more liquid by reason of having the cash rather than the securities. The appellees gained nothing. The public deposit or its proceeds was used, or will be used, for the payment of general creditors of the bank. No more than an equal amount of the pledged notes will be withheld. The action sounds in equity.

> The general creditors of the bank or the appellant, their representative (the receiver), cannot be heard to say that the pledging of the securities was illegal while they retained the benefits of the transaction. Melaven v. Hunker et al., 35 N. M. 408, 299 P. 1075. It would be unconscionable to permit general creditors to profit where they had no loss, at the expense of the appellees, who have profited nothing and have done no wrong. It must not be permitted unless there is some insuperable rule of law which requires it'' (page 112).

In response to the receiver's contention that he may disaffirm the pledge agreement and retain the bonds without returning the railway company's deposits (pages 27-33), we respectfully call the Court's attention to the latter part of the foregoing quotation from *Schornick v. Butler*, and to the decision of the Court of Appeals of New York, in *State Bank of Commerce of Brockport v. Stone, 184 N. E. 750*, (cited by respondent, page 27). That Court following some of the cases cited by respondent, including *Baltimore & Ohio v. Smith*, held that a state bank had no authority to pledge its assets to secure a private deposit. But the Court required the superintendent of banks to return the deposits as a condition precedent to his recovery of the pledged bonds. After holding the pledge agreement void, the Court of Appeals stated:

> ''This does not necessarily mean, however, that the the judgment of the courts below must be reversed, as we have to consider the effect of ultra vires. In pledging these bonds, the officers were acting for and on behalf of the bank, and for its business, apparently seeking to obtain deposits which, under the Banking Law, it was authorized to receive. They applied the deposits to the bank's business, and the bank has had and re-

ceived the benefit of the money due to the agreement which the bank made, and the bonds which it delivered as security. Under these circumstances, it would not be just for the bank or its creditors to accept all the benefits and repudiate the burdens, unless the acts of the bank be in violation of some direct and positive statute. Whatever the difference of view there may be as to the effect of ultra vires on corporate contracts, in no jurisdiction can a party retain what it has received under such a contract and refuse to perform the contract."

In this connection, we note that this Honorable Court in *Eastern Building and Loan Association v. Williamson, 189 U. S. 122, 47 L. ed. 735,* approved the following statement by the Court of Appeals of the law of New York:

"We deem it unnecessary at this time to determine whether the defendant was authorized by that statute to enter into such contracts, for, if we assume that the making of them was in excess of the express power conferred upon the corporation by that statute, still, as the contracts involved no moral turpitude and did not offend any express statute, they were not illegal in a sense that would prevent the maintenance of an action thereon. It is now well settled that a corporation cannot avail itself of the defense of ultra vires when the contract has been, in good faith, fully performed by the other party, and the corporation has had the benefit of the performance and of the contract. As has been said, corporations, like natural persons, have power and capacity to do wrong. They may, in their contracts and dealings, break over the restraints imposed upon them by their charters; and when they do so their exemption from liability can not be claimed on the mere ground that they have no attributes or facilities which render it possible for them thus to act. While

they have no right to violate their charters, yet they have capacity to do so, and are bound by their acts where a repudiation of them would result in manifest wrong to innocent parties, and especially where the offender alleges its own wrong to avoid a just responsibility. It may be that, while a contract remains unexecuted upon both sides, a corporation is not estopped to say in its defense that it had not the power to make the contract sought to be enforced; yet, when it becomes executed by the other party, it is estopped from asserting its own wrong, and cannot be excused from payment upon the plea that the contract was beyond its power" (U. S. p. 129, L. ed. 741)

We deem it appropriate to quote the concluding paragraphs of the opinion in *State Bank of Commerce Brockport v. Stone, supra*:

"One word, however, remains to be said regarding the effect of this decision, which is stated to be a test case. By no means do we hold that, although banks have no implied authority to pledge their securities for private deposits, yet after the thing is done it cannot be undone. In this particular case the bank became insolvent and was taken over by the superintendent of banks. His duties, however, do not begin with insolvency. Our Banking Law has many provisions seeking to preserve the solvency of banks, and secure depositors. Thus section 39 makes it the duty of the superintendent to examine banks twice a year. 'On every such examination inquiry shall be made as to the condition and resources of such corporation, banker or broker, the mode of conducting and managing its affairs, the actions of its directors or trustees if a corporation, the investment of its founds, the safety and prudence of its managment, the security afforded to those by whom its engagements are held, and whether

the requirements of its charter and of law have been complied with in the administration of its affairs; and as to such other matters as the superintendent may prescribe.'

"Section 56 prescribes: 'Whenever it shall appear to the superintendent that any corporation * * * has violated its charter or any law, or is conducting its business in an unauthorized or unsafe manner, he may issue an order directing the discontinuance of such unauthorized or unsafe practices,' and in case of its failure to comply, he is authorized by section 57 to take possession of the business.

"The superintendent, therefore, is not compelled to wait until insolvency to interfere with the pledging of a bank's securities for private deposits. It is his duty to ascertain the facts, and in such manner as to him seems advisable, and at such time as comports with the necessity of the occasion, compel banks to again retake their assets, if so pledged, upon the return of the deposits, when demanded." (pp. 754-755)

The authority conferred upon the Comptroller of the Currency with reference to national banks, is substantially the same as that conferred upon the Superintendent of Banks of the State of New York. In the instant case the Comptroller's bank examiners learned of the pledge of liberty bonds to the railway company one month before the bank's failure, but made no complaint of the transaction (R. 94-95). Had they, or the Comptroller, then complained, while the bank was solvent, the railway company

could have withdrawn its deposits and have avoided its now threatened loss.

Dated at Washington, D. C., December 6, 1933.

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CHARLES ELMORE

Supreme Court of the United States

OCTOBER TERM, A. D., 1933

No. 128

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Appellant,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas, *Appellee.*

REPLY BRIEF ON BEHALF OF S. O. POTTORFF, RECEIVER OF THE FIRST NATIONAL BANK OF EL PASO, TEXAS

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Supreme Court of the United States

OCTOBER TERM, A. D., 1933

No. 128

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Appellant,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas, *Appellee.*

REPLY BRIEF ON BEHALF OF S. O. POTTORFF, RECEIVER OF THE FIRST NATIONAL BANK OF EL PASO, TEXAS

ABSTRACT AND STATEMENT OF THE CASE

The statement of the pleadings, of the evidence and of the proceedings in the Trial Court and in the Circuit Court of Appeals as made by Appellant is sufficient to acquaint this Court with the nature of the suit and with the character of the questions which are involved.

ARGUMENT

Introduction

There are three questions involved in this appeal.

I. Did the First National Bank have the power to pledge a portion of its assets to secure the payment of the private deposits made by the Texas and Pacific Railway Company?

2. Can the receiver of the First National Bank assert the invalidity of the pledge?

3. Does any basis exist for granting the Texas and Pacific Railway Company a preferred claim against the receiver for the amount of its deposit balance?

A. THE FIRST NATIONAL BANK, UNDER THE NATIONAL BANKING LAWS AS THEY EXISTED IN JANUARY, 1931, AND THEREAFTER, HAD NO POWER TO PLEDGE THE LIBERTY BONDS INVOLVED IN THIS SUIT TO SECURE THE PAYMENT OF THE PRIVATE DEPOSITS OF THE TEXAS AND PACIFIC RAILWAY COMPANY. THE ATTEMPTED PLEDGE WAS VOID.

I. No express power has been conferred on national banks to pledge assets to guarantee the payment of private deposits.

All national banks are organized under and governed by the provisions of the laws of the United States. The corporate powers of a national bank were prescribed by Section 8 of the National Banking Act of 1864 (Act of June 3, 1864, c. 106, Stat. 101, now U. S. C. Tit. 12, Sec.

24; R. S., Sec. 5136), which provides that such a bank shall have power to adopt a seal, to have succession for ninety-nine years, to make contracts, to sue and be sued, to elect directors and officers, to prescribe by-laws and

> "Seventh. To exercise by its board of directors, or duly authorized officers or agents, subject to law, *all such incidental powers as shall be necessary to carry on the business of banking;* by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; *by receiving deposits;* by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this chapter."

It is settled that the provisions of this act as to discounting notes, receiving deposits, etc., are to be read as descriptive of the kind of banking which is authorized and as illustrative of incidental powers. *First National Bank of Charlotte v. National Exchange Bank of Baltimore,* 92 U. S. 122 (1875); *Western National Bank v. Armstrong,* 152 U. S. 346 (1894). It follows that the incidental powers granted by the act are not those incidental to receiving deposits, etc., but are those "necessary to carry on the business of banking." Thus it has been said in *Logan County National Bank v. Townsend,* 139 U. S. 67, on 73 (1891):

> "that the national banking act is an enabling act for all associations organized under it, and *that a national bank cannot rightfully exercise any powers except those expressly granted by that act, or such incidental powers as are necessary to carry on the business of banking for which it was established.*" (This statement has been quoted or referred to with approval in all subsequent cases.)

There is no express statutory provision which grants national banks the power to pledge assets as security for

private deposits; therefore, if the power exists, it must be by virtue of the incidental powers.

II. National banks do not have implied power to pledge their assets to guarantee the payment of private deposits.

In determining what powers are "necessary to carry on the business of banking," we may well adopt as a general statement the definition of Mr. Chief Justice Marshall when he said that, necessary, "imports no more than that one thing is convenient, or useful, or essential to another."[1] But, this quotation must be taken along with the more directly appropriate language of Mr. Chief Justice Waite, who, after quoting paragraph seventh of the National Banking Act of June 3, 1864, which reads as follows:

> "Seventh. To exercise by its Board of Directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this Chapter;"

said:

> "Authority is thus given to transact such a banking business as is specified, and all incidental powers necessary to carry it on are granted. These powers are such as are required to meet all the legitimate demands of the authorized business, and to enable

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1 McCullough v. Maryland, 4 Wheaton 216, 412; 4 Law Ed. 579, 603.

the bank to conduct its affairs within the general scope of its charter, *safely and prudently.*"[2]

We should also take direction from the language in *Thomas v. West Jersey Railroad Company*, 101 U. S. 71; 25 Law Ed. 950. Mr. Justice Miller said:

> "That principle is, that where a corporation, like a railroad company, has granted to it by charter a franchise intended in large measure to be exercised for the public good, the due performance of the functions being the consideration of the public grant, any contract which disables the corporation from performing those functions which undertakes, without the consent of the state, to transfer to others the rights and powers conferred by the charter, and to relieve the grantees of the burden which it imposes, is a violation of the contract with the state, and is void as against public policy."

It is true that in the cited case the corporation had sought by a lease to deprive itself of performing its duties to the public. But the reasoning is sufficient to justify us in saying that a power, which, if exercised by a bank, would be calculated to disable and prevent a bank from performing its important duties to the public, should not be considered necessary. An act which is not authorized by the express terms of a statute, and which is calculated to render a bank unsafe and incapable of performing its proper functions, is against public policy.

Some of the opinions which we shall cite hold that the securing of private deposits by the pledging of bank assets is void because against public policy. We say that such an act, if it is destructive of sound banking, is not useful or essential, is not necessary, and is therefore not within the authority conferred by implication.

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2 First National Bank of Charlotte v. National Exchange Bank, 92 U. S. 122; 23 Law Ed. 679, 681 (1875).

(a) **THE PLEDGING BY BANKS OF THEIR ASSETS TO SECURE PRIVATE DEPOSITS IS NOT HELPFUL IN OBTAINING AND RETAINING PRIVATE DEPOSITS AND IN RENDERING THE TRANSACTION OF THE BANKING BUSINESS SAFE AND PROFITABLE.**

National banks have become charged with a public interest. They are carefully regulated by statute and by numerous safeguarding regulations of the Treasury Department, administered by the Comptroller of the Currency. It is a far cry from the private banker of old England to the modern institution of today. Banks in these days must publish at stated intervals reports which show the nature of their assets and liabilities.

As they are now prepared, these reports make no mention of pledges which may have been made to secure individual private deposits. The public is led to believe that all of the particular bank's assets, except such as may, in accordance with law, secure public deposits, stand as security for the payment of all private deposits, without preference, and upon the strictest equality. If present publication regulations are continued, and pledges are made to secure private deposits, such pledges will be made in secret so far as the public is concerned. The result is the perpetration of the grossest fraud on the unsecured creditors of the bank.

Opposing counsel may reply by adopting the views expressed in the dissenting opinion of Circuit Judge Alschuler in *Sneeden v. City of Marion*, 64 Fed. (2d) 721, 731. He said:

> "It is pointed out, in support of such a public policy of the state, that ordinarily there is secrecy in such pledges of which the general public has no notice, and that depositors not so secured would usually have no means of knowing how much of the bank's reported assets are so segregated.

"It seems to me that the vice is not with the pledging of the assets, but with the laws and regulations concerning reports and advertisements of banks. I fully agree that banks should be required to make frequent public reports of their condition, and that in such reports it should be specifically disclosed what part of the reported assets is so pledged. To my mind it is a vicious practice to permit banks to advertise their 'resources' at an amount inclusive of their total deposits, without requiring that at the same time, and quite as prominently, there be stated the liabilities to which the resources are subject."

But suppose a bank should be required to publish the nature and extent of its pledges of assets to secure private deposits. No bank, in good times, and with its own affairs in excellent condition, would care to invite the practice by publishing notice that some of its private depositors had demanded and obtained securities. If times were hard, and if the bank were anxious to retain its larger depositors, and if the practice were generally recognized as legal, the bank would, in certain instances, be required to make pledges of its assets. The publication of its next statement would advise the public of what had taken place. The demand for security would become general. The ultimate effect would be ruinous to the bank and disastrous to unsecured and partially secured creditors.

Another specious argument is frequently made. It is said that the bank and its creditors are not injured by the pledging of its assets, that the bank receives in cash the same amount as the amount of the debt for which the bank's assets are pledged. It is said that upon the return of the money the pledged assets are released. Let us examine into this claim. Of course, if the pledged assets consist of Liberty Bonds, and if they have at all times a ready sale at par, the argument might seem to be of some

merit. But if the power to pledge exists, a bank may pledge any character of asset, and the pledge agreement may contain the strict provisions usually found in such instruments. It is easily conceivable that when the practice becomes recognized and general, a bank might be required to pledge the personal notes of its customers of $150,000.00 to secure a demand deposit of $100,000.00. The pledge agreement might provide for sale on ten days' notice. Suppose a number of such instances. It is not hard to picture the plight of the unsecured creditors in the event of insolvency.

Circuit Judge Alschuler, in his dissenting opinion in *Sneeden v. City of Marion*, supra, says:

> "It is also pointed out that such pledging of a bank's assets may in case of the bank's threatened disaster, enable certain depositors to be favored as against others. This, of course, would bring into the picture collusion and probably fraud, which would be dealt with when it appears. . . . ."

The learned judge does not take into account the fact that the effect of non-fraudulent and perfectly valid pledges would be as vicious and as disastrous in result to unsecured creditors as those made with knowledge of insolvency. Neither does he consider the practical difficulty involved in proving actual fraud and knowledge of insolvency.

We here mention the results to unsecured creditors of allowing a bank to pledge its assets to secure private deposits for the reason that the public will not be unmindful of the danger. With such knowledge, no depositor would be so careless of his own interest as to remain quiescent while his fellows were demanding and receiving security. Moreover, no man will for long continue to do his banking business with an institution where

he must constantly watch the value of the collateral securing his deposit.

When we turn to the other side of the picture, we see that no bank can do a profitable business if a substantial portion of its assets are frozen in pledges.

That the practice under examination is neither necessary nor helpful is made evident by the fact that during the long history of national banking in this country no case directly raising the question of the validity of such pledges has heretofore arisen to be decided by this Court, and no such question was directly presented in the Federal Courts prior to the case of *Smith against Baltimore and Ohio Railroad Company,* decided in the District Court, Western District of Pennsylvania, March 5, 1931. It might be said that for a long period no case arose in the Federal Courts involving the validity of a pledge of assets to secure public deposits. This is of little significance, because the Comptroller always recognized such pledges as valid. His receivers, acting under his instructions, did not question their validity, and there was therefore no opportunity of raising the question in the Federal Courts prior to the enactment of the Amendment of June 25, 1930.

The testimony of Appellant's witness, J. E. Benton, is significant on the question of the necessity for this practice. He testified in part as follows:

> "My name is J. E. Benton. I was formerly vice-President and Cashier of the First National Bank here in El Paso. I was connected with that Bank since February, 1903." (P. 63, R.)

He also testified:

> "The bank furnished surety company bonds to secure deposits. We guaranteed deposits by surety bonds. I would imagine that the bank had between

6,000 and 7,000 depositors. Out of those 6,000 or 7,000 deposits there were maybe six or eight or ten deposits secured by a surety bond at any one time, excluding the Government, and such accounts as that. It was the custom of the bank to give security to a few of the corporations, six or eight or ten. I think that a great many of the corporations insisted on it, and some paid the premiums themselves, and others we paid the premiums on, but those that paid the premiums would exceed that six or eight or ten I mentioned. Those instruments were in the form of surety bonds. It was not a pledge of the assets of the bank. *As far as I can remember this is the only case where a private account was secured by pledging the assets.*" (Page 74, R).

And, it must be borne in mind that this instance did not take place until the heavy withdrawals, which closed the bank, had begun.

This is a strong indication that such a practice was not necessary to the conduct of the banking business. Moreover, whenever it becomes known that certain private depositors of a bank are insisting upon, and obtaining, a pledge of the bank's assets to secure payment of their deposits, other depositors are led to demand similar security. If the practice continues, it eventually ties up the assets of the bank, and destroys the bank's usefulness.

The primary functions of a bank are to accumulate and to lend money. If each depositor insists upon his deposit being guaranteed by the pledge of collateral, the bank's ability to lend, and thereby earn a profit, is seriously impaired. By such a practice, public confidence in the integrity of the bank is destroyed, and its usefulness ends.

Moreover, if such practice is allowed, the large and alert depositors are protected, and, in event of insolvency, the small unsecured depositors are discriminated against.

If such practice is allowed, public bank statements showing assets available for the protection of depositors become a deceit and a fraud. Certainly, any practice which cannot stand publicity and which impairs and ultimately destroys the bank's usefulness, cannot be a necessary incident to the business of banking.

(b) THE RULINGS AND PRACTICE OF THE UNITED STATES TREASURY DEPARTMENT INDICATE THAT THE PLEDGING OF SECURITIES TO GUARANTEE PRIVATE DEPOSITS IS NOT NECESSARY TO THE BUSINESS OF BANKING.

Appellant's contention is that it is necessary for banks, in order to carry on their business, to give security for private deposits. Appellant then says that because of this assumed necessity, an implied power exists in banks to give such security. The conclusion is wrong, because the premise is unsound. Certainly, the Treasury Department, and more particularly the Comptroller, is qualified to judge of the necessity for the exercises of such a power by national banks. The Comptroller has consistently maintained the position that national banks have no such power. Attached as an Appendix are copies of letters showing the Comptroller's attitude.

In the case of *Baltimore and Ohio Railroad Company v. Smith, Receiver,* 56 Fed. (2d) 799, the Circuit Court of Appeals of the Third Circuit rendered an opinion fully supporting our contention in this case. In that opinion it was stated:

> "There is no evidence showing that it is necessary. On the other hand, inference is fairly reasonable that thousands of successful banks have never exercised such power. It cannot be concluded from the evidence that the exercise of such power is necessary in order to carry on the business of banking successfully. It is admitted that whenever the Comptroller was asked for an opinion as to the

power of national banks to pledge collateral to secure private deposits, in every instance, he has disapproved of such pledges and held that, in his opinion, national banks do not have that power. Such uniform and long continued interpretation and practice of an act by the Department charged with administering it has great weight, and is persuasive as to its correct construction."

And, in the Agreed Statement of Facts in that case it is said:

> "However, during, before and after the said period of February 23, 1928, to July 31, 1930, when the said Comptroller was requested by national banks or others for an opinion upon the power of national banks to pledge securities to secure a private depositor, in every instance the Comptroller disapproved of such pledging by stating that, in his opinion, national banks had no such power."

The Comptroller of the Currency is charged with visitorial duties over national banks; he is charged with the execution, administration, and application of the banking laws. Therefore, his construction or interpretation of the banking laws is entitled to great weight.

The attitude of the Treasury Department was shown when the Act of June 25, 1930, amending Section 45 (R. S. 5153) of the National Banking Act was passed. The acting Secretary of the Treasury wrote to the Committee which had the bill under consideration as follows:

> "While the office of the Comptroller of the Currency has consistently taken the position that national banks have the right to give security for the safekeeping and prompt payment of public monies of the state or other political subdivisions thereof, deposited with such national banking associations, several recent decisions have thrown some doubt on this question, with the result that in some states the

state banks may secure the public deposits, but the officers of the state are in doubt about depositing with the national banks in the absence of any specific law by Congress on the subject. It would be extremely helpful, therefore, if it is possible for your Committee to report out, and the House pass, S. 486."

The Supreme Court has this to say with reference to the interpretation by an executive department of a law of Congress:[3]

> "Even if the meaning were not otherwise made plain, we should be slow to reject the construction thus put on the section by the head of the Department charged with administering it."

And again:[4]

> "So, even if there was some uncertainty in the Act, we should regard this long continued and uniform practice of the officers charged with the duty of administering it as persuasively determinative of its construction."

So, in our case, the administrative official charged with enforcing the banking laws of the United States has denied to national banks the power to pledge assets as security for private deposits. Because of *dicta* in some Court decisions casting doubt upon the power of national banks to protect public deposits, the amendment of 1930 was passed.

The failure of Congress to say anything with reference to private deposits adds very materially to the weight

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3 Kern River Co. v. U. S., 257 U. S. 147 on 154 (1921); other authorities to the same effect are Corsicana National Bank v. Johnson, 251 U. S. 68 on 83 (1919); First National Bank in St. Louis v. State of Missouri, 263 U. S. 640 on 652 (1925); 25 R. C. L. 1043, Section 274.

4 U. S. v. Minnesota, 270 U. S. 181, on 205 (1926).

to be given to the Comptroller's interpretation with reference to securing private deposits, and would seem to amount to a distinct recognition by Congress of the correctness of the Comptroller's view. The long continued construction put upon the national banking act by the Comptroller, concurred in by Congress, is conclusive that the power to pledge assets to protect a private deposit does not exist.

But, it is said that in this case the Comptroller, acting through his examiners, had notice on August 6, 1931, that the Liberty Bonds involved in this suit had been pledged to secure the private deposit of The Texas and Pacific Railway Company, and that the Comptroller made no objection to such pledge. The testimony on this point was given by S. O. Pottorff. He testified:

> "I am the Receiver of the First National Bank here in El Paso. There were no examinations made by the bank examiners of the condition of the bank from the 29th day of January, 1931, until August 6, 1931. There was one examination made between the 29th of January, 1931, and September 6, 1931. That examination began at eight o'clock in the morning, August 6th, and ended at noon on August 20th. The examiner was Jacob Embry. I don't know the names of his assistants. I think Mr. Collier was here in charge, although I was not here." (Page 82, R.)

This witness also testified:

> "This report of the examination made in August, 1931, was not sent in to the Comptroller of the Currency until after the Bank had closed. I know that of my own knowledge." (Page 87, R.)

It is thus apparent that neither the Comptroller nor any of his examiners knew of this pledge until shortly before the Bank was closed, and that the Comptroller was never called upon to pass on the validity of this pledge.

(c) CONGRESS, BY PASSING THE ACT OF JUNE 25, 1930, SECTION 45 (R. S. 5153), MADE IT CLEAR THAT NATIONAL BANKS SHOULD THEREAFTER HAVE NO POWER TO PLEDGE THEIR ASSETS TO SECURE PRIVATE DEPOSITS.

We find the following statement in the brief filed on behalf of Illinois Central Railroad Company as Amicus Curiae in connection with the application for Writ of Certiorari in this case:

> "The statement of this amendment is not that security shall be given, but security *may* be given and it is therefore contended by the Receiver that as the act only grants authority to give security for the public moneys of a state or political subdivision thereof, therefore, it was the plain intention of Congress to withhold the power to give security for a private deposit. This is a plain *non sequitur* for the following reasons: In the first place, it was known that national banks did give security to private depositors and if Congress had intended to stop such practice it would have been prohibited by express enactment; second, the history of the passage of this Act of 1930 shows that it was passed merely to quiet doubts of some timid national bankers and to confirm in direct and positive statutory form a power (though already existing) to national banks so that they could compete with state banks, which were obtaining state deposits by giving security therefor."

We find the following statement in the brief filed on behalf of the Texas and Pacific Railway Company:

> "It thus appears that Congress, by amending section 90 of the National Bank Act to afford the specific relief sought, had no intention to and in fact did not define, amend or restrict any power granted to national banks by section 24 of that Act."

The report of the Senate Committee was based on a letter from the Attorney General of Minnesota which contained the following language:

> ". . . . The national banks of this State have pledged with the State and the various subdivisions thereof millions of dollars in Government and other bonds as security for public deposits. They are anxious to be permitted to do so, and we are willing that they should. Under the law as it now stands we may be taking a chance in accepting such pledges from the national banks, and we should like to have the chance removed by legislation in Congress which will specifically authorize such pledges by national Banks."

The House Committee had received a request from the Acting Secretary of the Treasury reading in part as follows:

> "While the office of the Comptroller of the Currency has consistently taken the position that national banks have the right to give security for the safe-keeping and prompt payment of public moneys of the State or political subdivision thereof deposited with such national banking associations, several recent decisions have thrown some doubt on this question with the result that in some States the State banks may secure the public deposits, but the officers of the State are in doubt about depositing with the national banks in the absence of any specific law by Congress on the subject. It would be extremely helpful therefore, if it is possible for your committee to report out, and the House pass, S. 486."

Counsel for the Illinois Central Railroad Company say:

"In the first place, it was known that national banks could give security to private depositors, and if Congress had intended to stop such practice, it would have been prohibited by express enactment."

There is nothing to indicate that Congress knew that banks were giving security for private deposits. On the contrary, Congress knew that the banks had seldom sought to guarantee private deposits, and knew that the Comptroller had consistently ruled that no such authority existed. The banking fraternity also knew this to be a fact. It was also known that the great weight of modern authority was to effect that banks did not have the right to pledge assets to secure private deposits. If Congress had intended that national banks should have unrestricted authority to pledge assets to guarantee all deposits, both public and private, it would have been a simple matter to have adopted an act reading:

"National banks shall have authority to pledge their assets to secure the payment of deposits."

This would have been broad enough to have given national banks every authority held by state banks, and would have left intact any supposed additional authority in national banks to guarantee generally both public and private deposits. Congress, however, was unwilling to go that far. It was not even willing to grant general authority to pledge assets to secure public deposits. It gave to national banks the right to pledge assets to secure public deposits, with the limitation that such security should be "of the same kind as is authorized by the law of the state in which such association is located in the case of other banking institutions in the state."

The doctrine of "expressio unius est exclusio alterius"

is applicable here.[5] Moreover, the language in *State ex rel. v. First National Bank*, 249 S. W. 619 (Missouri—1923), affirmed in *First National Bank v. Missouri*, 263 U. S. 640 (1924), reading:

> "Despite this fact where, as here, there is a general grant of power, however clear that grant may be, the enactment of subsequent legislation containing a specific kindred grant of power will afford at least persuasive support to the conclusion that the latter was not included within the former or the original grant. Such is the effect of the Act of Congress of March 3, 1865, Section 5155, 3 U. S. Comp. Stats. 1901, p. 3467, now U. S. Comp. St. Section 9695. This Act provides that any bank or banking institution organized under a state law and having branches, may in conformity with existing law become a national bank and retain its branches. In the passage of this act it is evident that the legislative construction of the original is that it did not authorize the establishment of branch banks. Otherwise, the subsequent Section 5155 would not have been enacted."

is in point.

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5 25 R. C. L., Section 229, page 981: " 'Expressio unius est exclusio alterius' is a universal maxim in the construction of statutes"; U. S. v. Arredondo, 8 Law Ed. 547, 560, 6 Peters 691; "If Congress had intended to exempt any other articles of growth or production of those countries, the articles would have been enumerated and included in that exception, 'expressio unius est exclusio alterius'," Sturges vs. Draper, 20 Law Ed. 255, 258, 12 Wallace 19; "Thus enumeration of the purposes for which the corporation could acquire title to real estate must necessarily be held exclusive of all other purposes," Case vs. Kelly, 33 Law Ed. 513, 515, 133 U. S. 21; "But when we consider the general rule that the affirmative description of the cases in which the jurisdiction may be exercised implies a negative on the exercise of such power in other cases . . . ," In Re Thomas Heath, 36 Law Ed. 358, 359, 144 U. S. 92; "If . . . . the powers conferred are expressly enumerated, this, under the maxim of 'expressio unius est exclusio alterius,' implies the exclusion of others not enumerated," State vs. Missouri Athletic Club, 170 S. W. 904, 909.

(d) ANSWER TO SOME OF THE REASONS GIVEN IN SUPPORT OF THE POWER OF BANKS TO PLEDGE ASSETS TO SECURE PRIVATE DEPOSITS.

(1) There is an essential difference between a deposit and a loan.

The argument most often advanced in favor of the power to pledge is supposed analogy between a loan and a deposit, and Appellant urges this argument in its brief. In a recent law review note[6] the able author thus states and answers the argument:

> "It is now conceded law that a bank has the corporate power to borrow money and to hypothecate its assets to secure the loan. Arguing with this point as a premise, many of the courts sustaining the majority view have used the following syllogism:
>
> (1) A bank may pledge its assets to secure a loan; (2) a deposit is, as a matter of law, a loan; (3) therefore, a bank may pledge its assets to secure a (public) deposit. This has been a favorite argument, and much verbiage has been spent upon it. The fault lies in the minor premise, for a deposit is most clearly not a loan. While it is true that the result of both transactions is the relationship of debtor and creditor, that is the only similarity between the two, and apart from this the two are different to their very roots. The reasoning that a deposit and a loan are the same results from accentuating this sole similiarity between the two. That a debtor-creditor relationship results from both transactions is mere *legis accidens*, and by no means warrants the conclusion that the two are alike for all purposes."

In a Minnesota case, *Farmers and Merchants State Bank of Ogilvie v. Consolidated School District*, 219 N. W. 163,

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6 Bernard F. Cataldo in 79 U. of Pa. L. Rev. 608, on 614 (1931).

65 A. L. R. 1407, (Minn., 1928) the Court refers to an opinion from another state based on the analogy between loans and deposits, and answers the argument thus:

> "The essential premise of that opinion is that, with respect to the power to give security, bank deposits and bank borrowings are alike. That seems to us unsound. Bank deposits and bank borrowings are alike in but the one respect that one result of each is the relation of debtor and creditor. In every other respect the two operations are not only different but in complete antithesis. *Deposits are attracted by the strength of a bank, whereas its borrowings are compelled by weakness or other adverse circumstance.* (The borrowing of money has been said to be 'so much out of the course of ordinary and legitimate banking as to require those making the loan to see to it that the officer or agent acting for the bank had special authority to borrow money.' Western National Bank v. Armstrong, 152 U. S. 346.) Large deposits signify health and large borrowings bank disease. Springing from opposite causes, the two by their existence signify opposite conditions—deposits the normal and borrowings the abnormal. Moreover, the anthithesis holds to the end, for the withdrawal of a deposit is a loss whereas the payment of a loan is a gain. Deposits continued and increased evidence banking success, whereas, borrowings continued and increased portend failure. Save in the relation of debtor and creditor common to both, the two are different in their every incident—not only different but opposed in origin, in purpose, and in effect. *How it comes then that the obvious truth that a bank may pledge collateral for borrowed money can be used to sustain the same power in the case of deposits we cannot understand. The former is clearly necessary, usual and incidental; whereas the latter is neither necessary, usual or incidental, but is positively dangerous.* Therefore, we repeat, we consider it not possessed by any state bank in

Minnesota. It is not an express power and clearly not included among those implied."

So, in a North Dakota case, *Divide County v. Baird*, 212 N. W. 236, 51 A. L. R. 296, (N. D., 1926), the argument is answered thus:

> "The doctrine that there is no difference between a loan and a deposit we cannot accept in all its implications. It is true that in law the two transactions have many characteristics in common; but so have other business deals which, nevertheless, are not identical in all their legal incidents. The striking fact remains, a fact which this court cannot ignore, that a real difference between a deposit and a loan has always been assumed, as a matter of custom, in the banking business itself, and in all legislation dealing with the subject since statehood.
>
> "We are warranted in taking judicial notice of the fact that, in the banking business, it has been and still is customary to treat loans and deposits as distinct and essentially dissimilar transactions. Without going into details, this fact is evidenced by methods of bookkeeping and of making reports of the financial condition of the bank, both to private individuals, through the press or otherwise, and to the public examiner.
>
> * * * * *
>
> "We think the conclusion necessarily follows that there is such a distinction between a deposit and a loan of money that no helpful analogy can be drawn, with respect to the power to pledge paper to secure a deposit, from the fact that the assets of a bank may be pledged to secure a loan."

Of course there is no doubt that all banks, under certain circumstances, can borrow money and give security therefor. But the Courts expressly say that the business of a bank is to lend and not to borrow money, and that

the power to borrow can be exercised only when a bank is embarrassed, or when large sums of money must be raised in sudden contingencies. It is to be noted that the power to borrow is granted solely to protect investments and assets (which constitute the depositors' protection) and not to procure money with which to make new investments. In other words, borrowing is permitted because it is necessary to protect depositors, and only then. But the pledging of assets in order to procure or retain a deposit is an entirely different thing; instead of protecting depositors, it distinctly prejudices them, and it violates the bank's duty of equal, fair and uniform treatment of all depositors.

In this connection, it has sometimes been argued that the mass of depositors cannot complain against a pledge to secure a deposit because the assets withdrawn and pledged are replaced by the deposit. The argument is thus answered:[7]

> "There has also been a suggestion advanced in two or three cases that the private depositor has no complaint against such pledging because the amount received as a deposit is equal to the assets hypothecated. *En bref*, that portion carved out of the bank's assets by a pledge to the depositor is replaced by the deposit. While this answer to the matter is tinged with the semblance of persuasion, it is not satisfactory. In the first place, it is quite manifest that the depositor may well require more security than an amount which will barely cover his deposit. Secondly, the assets are clearly the bank's property, whereas the deposit received is not, notwithstanding the 'legal title' is in the bank, since the depositor

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7 B. F. Cataldo in 79 U. of Pa. L. R. 608, (1931) on 616.

may draw thereon. While the pledge remains static, the amount of the deposit may dwindle, and matters are allowed to remain in *statu quo* by the bank, in the hope that *carus cliens* will soon swell his deposit; and in the meantime the bank has virtually deprived itself of a profitable slice of its property, to the detriment of its private depositors. Further, it must be borne in mind that the validity of the pledge is assailed only *after the bank has become insolvent.* This contention, as well as others advanced in support of the majority rule, oblivious of this fact, seems to be based on the thought that the validity of the transaction is to be determined primarily from looking at the conditions existent either when the pledge was made, or the private customer deposited his money with the bank. Naturally, while the bank is in good condition, there is little fault to find with such a pledge. However, the bank may well pledge its assets after it has received the private customer's deposit; and above all, the very reason why the pledge should be condemned is because of the everpresent contingency that the bank may become insolvent, and because in that event the unsecured depostors are deprived of assets which should go to the payment of their claims. Therefore, when, after the insolvency of the bank, the court is called upon for the first time to pass upon the validity of the pledge, it is futile to look at the transaction as one isolated in time, or to try to determine by segregation into temporal compartments that which should not be so treated."

(2) There is a basis for discriminating between public and private deposits.

Cases may be cited where, even in the absence of statute, banks have been allowed the right to pledge their assets to secure public deposits. There is a real distinction. Originally, at common law, the sovereign had pre-

ference over other creditors of an insolvent bank.[8] The opinion in the above case by the Court of Civil Appeals was reversed by the Supreme Court of Texas,[9] but the Supreme Court recognized the preference accorded the sovereign under the common law.

Some of the Courts sustaining public pledges are influenced by the old doctrine of the prerogative right granting to the state priority in distribution, and the argument has been stated thus:

> "If then, the state is ultimately to have a preference, what difference does it make whether it realizes the enjoyment of this preference by force of its prerogative right of priority after the insolvency of the bank, or by receiving a pledge of the assets from the same bank, and enforcing the same after the failure of the latter? The result to the other depositors is identical." [10]

The public has an interest in having public funds paid. This interest has very generally been recognized as a reason for granting a preference in favor of public funds, sometimes by statutes expressly authorizing such preference, and sometimes by judicial construction permitting it. The reason for the rule in the case of public deposits is absent in the case of private deposits. Custom and the requirements of competition may have rendered it advisable and necessary to give security for public deposits. Quite the contrary is true in the case of private deposits.

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8 State Bank of Commerce v. U. S. F. & G. Co., 28 S. W. (2d) 184.

9 48 S. W. (2d) 974.

10 79 U. of Pa. Law Review, 608 on 619 (1931).

(e) DISCUSSION OF AUTHORITIES.

So far as the decision of the Federal Courts are concerned, the only case directly in point with which we are familiar is *Smith v. Baltimore and Ohio Railroad Company,* 48 Fed. (2d) 861, affirmed by the Circuit Court of Appeals of the Third Circuit, 56 Fed. (2d) 799. That decision fully sustains our contentions in this case. The Court will find the opinion of the Trial Court, in 48 Fed. (2d) 861, very full and complete, with logical answers to all of the contentions made by the Railroad Company.

The case of *Sneeden v. City of Marion,* 64 Fed. (2d) 721, decided April 25, 1933, by the Circuit Court of the Seventh Circuit, while it deals with a public instead of a private deposit, fully sustains our views in this case, and refutes all of the arguments presented by opposing counsel.

In the opinion in the case of *Parks v. Knapp,* 29 Fed. (2d) 547, decided by the Circuit Court of Appeals, Eighth Circuit, November 19, 1928, we find these statements:

> "National banks are authorized to receive deposits. Their express power on that subject stops there. That is one of their principal functions and business. Morse on Banks and Banking (5th Ed.) Vol. 1, Sec. 48, says:
>
> > 'The banking powers are those which are either fundamental parts of the business, or have become so linked with them as to be identified with the exercise of the banking franchises.'
>
> "We are not advised that the transfer of a bank's assets to secure a depositor has become a general custom and thus so linked in practice with its express powers as to be recognized in the banking business as an incidental or implied power. We are inclined to believe with the Kentucky Court of Appeals and the Supreme Courts of Minnesota and North Dakota

that such a practice is not in keeping with sound banking methods, can only result in unfair discrimination and preferential treatment of its depositors, and ought not to be judicially approved. It enables those who are wary, usually because of large deposits, to gain advantage over the great number of small trustful depositors, and thus public confidence in banking institutions is shaken, to the public's detriment."

The decision, however, is based upon another point, and the quoted remarks must be classed as *dicta.*

Appellant relies upon the opinion of the Circuit Court of Appeals of the Fourth Circuit in the case of *Burrowes v. Nimrocks,* 35 Fed. (2d) 152. This case, in effect, upheld a pledge of assets to secure a call loan, rather than a public deposit. The Court spoke of the transaction as follows:

> "It was more nearly analogous to a call loan than to an ordinary deposit."

Appellant also relies upon an opinion by the same Court in the case of *Schumacher v. Eastern Bank and Trust Company,* 52 Fed. (2d) 925. It is true that in that case there is an expression by the learned judge who wrote the opinion to the effect that there is no valid distinction between pledging assets to secure a private deposit, and pledging assets to secure a public deposit. This expression was merely *dicta,* for the Court says:

> "But, without deciding what would be the rule in the case of an ordinary private deposit, we are satisfied that deposits by a bank, such as those involved here, made as loans to, and for the accomodation of, the bank in which they are made, do not come within that category."

We also call the Court's attention to the fact that both of these opinions by the Fourth Circuit had to do with

facts occurring prior to the amendment of June, 1930. Congress had not yet, by passing this amendment, indicated its views that under pre-existing law such pledges were not allowed, nor had Congress, by such amendment impliedly prohibited pledges other than those authorized by the amendment.

The following well considered cases from State Courts fully sustain our contention: *Austin v. Lamar County,* 26 S. W. (2d) 1062; *Foster v. City of Longview,* 26 S. W. (2d) 1059; *Arkansas-Louisiana Highway Association v. Taylor,* 6 S. W. (2d) 533; *Commercial Bank and Trust Company v. Citizens T. & G. Company,* 45 L. R. A. (N. S.) 950, 156 S. W. 160; *Divide County v. Baird,* 212 N. W. 236; *State Bank of Commerce v. Stone,* 184 N. E. 750 (New York, 1933).

B. THE RECEIVER IS NOT ESTOPPED FROM ASSERTING THE INVALIDITY OF THE PLEDGE AND IS ENTITLED TO RETAIN THE BONDS FREE OF THE PLEDGE.

I. Authorities sustaining our contention:

Corpus Juris has this to say with reference to the rule in the Federal Courts in Volume 14A, page 580:

> "According to the view held by the Supreme Court of the United States, and many of the state courts, a contract which is ultra vires in the true sense as being outside of the object of its creation as defined in the law of its organization, is void. Under this view, no action may be maintained upon the contract itself, and the contract cannot be ratified by either party because it could not have been authorized by either; nor can any performance upon either side afford validity to the contract, or be the basis of any right of action upon it."

In *Central Transportaion Company v. Pullman Company,* 139 U. S. 24; 35 Law Ed. 55, 68, 69, the Supreme Court said:

> "A contract of a corporation, which is ultra vires, in the proper sense, that is to say, outside the object of its creation as defined in the law of its organization, and therefore beyond the powers conferred upon it by the Legislature, is not voidable only, but wholly void, and of no legal effect. The object of the contract is, not merely that the corporation ought not to have made it, but that it could not make it. The contract cannot be ratified by either party, because it could not have been authorized by either. No performance on either side can give the lawful contract any validity, or be the foundation of any right or action upon it."

And,

> "A contract ultra vires being unlawful and void, not because it is in itself immoral, but because the corporation, by the law of its creation, is incapable of making it, the courts, while refusing to maintain any action upon the unlawful contract, have always striven to do justice between the parties, so far as could be done consistently with adherence to law, by permitting the property or money, parted with on the faith of the unlawful contract, to be recovered back or compensation to be made for it."

In *De La Vergne Refrigerating Company v. German Savings Institution,* 175 U. S. 40, 59, 44 Law Ed. 65, 72, the Supreme Court said:

> "The doctrine that no recovery can be had upon the contract is based upon the theory that it is for the interest of the public that corporations should not transcend the limits of their charters; that the property of stockholders should not be put to the risk of engagements which they did not undertake; that if the contract be prohibited by Statute, every-

one dealing with the corporation is bound to take notice of the restrictions in its charter, whether such charter be a private act or a general law under which corporations of this class are organized."

In *California National Bank v. Nat Kennedy,* 167 U. S. 362, 367, 371; 42 Law Ed. 198, 200, 201, the Supreme Court said, quoting from *Union and Pacific Railroad v. Chicago, R. I. and P. Railroad,* 163 U. S. 564:

> "A contract made by a corporation beyond the scope of its powers, express or implied, on a proper construction of its charter, cannot be enforced or rendered enforceable by the application of the doctrine of estoppel."

The opinion of the Supreme Court in *First National Bank v. Converse,* 200 U. S. 425, 50 Law Ed. 537, is to the same effect.

In the case of *Thomas v. West Jersey Railroad Company,* 101 U. S. 71, 25 Law Ed. 950, at 953, Mr. Justice Miller said:

> "And in regard to corporations, the rule has been well laid down by Comstock, Ch. J., in *Parish v. Wheeler,* 22 N. Y. 494, that the executed dealings of corporations must be allowed to stand for and against both parties when the plainest rules of good faith require it.
>
> "But what is sought in the case before us is the enforcement of the unexecuted part of this agreement. So far as it has been executed, namely: the four or five years of action under it, the accounts have been adjusted and each party has received what he was entitled to by its terms. There remains unperformed the covenant to arbitrate with regard to the value of the contract. It is the damages provided for in the clause of the contract that are sued for in this action; damages for a material part of the contract never performed; damages for the value of a

contract which was void. It is not a case of a contract fully executed. The very nature of the suit is to recover damages for its non-performance. As to this, it is not an executed contract.

"Not only so, but it is a contract forbidden by public policy, and beyond the power of the defendants to make."

So, in the case at bar, The Texas and Pacific Railway Company seeks "the enforcement of the unexecuted part of this agreement."

In the case of *B. & O. Railroad Company v. Smith, Receiver,* 56 Fed. (2d) 799, the Third Circuit of Appeals, in an opinion rendered March 10, 1932, said:

"The railroad has called on the bank or the receiver for its deposit. That it has the right to have and to that extent the bank is its debtor, but in the meantime the bank has become insolvent and is unable to pay in full. Accordingly the railroad must stand with, and not ahead of, the other depositors. All must share alike. The railroad now stands just where it would have stood had it continued as other depositors did, and not required the bank to do an unlawful act which is null and void. The agreement and deposit of these securities are of no effect, just as though they did not exist. Therefore the railroad must now be accorded the same treatment as other depositors and share pro rata with them. It cannot now take advantage of the illegal agreement and thus accomplish exactly what Congress sought to prevent by withholding power from national banks to pledge their assets to secure private depositors."

The holding of the Circuit Court of Appeals of the Seventh Circuit is to the same effect. *Sneeden v. City of Marion,* 64 Fed. (2d) 721 at 730, decided June 1, 1933.

In the case of *Foster v. City of Longview*, 26 S. W. (2d) 1059, the Commission of Appeals of Texas said:

> "With the illegal contract brushed aside, the City appears in the case merely as a depositor whose rights in the Bank's assets are no higher than those of other depositors."

And, in the case of *Austin v. Lamar County*, 26 S. W. (2d) 1062, it said:

> "The question arises as to the banking commissioner having the right to recover the notes from the possession of the county. If the rights of depositors other than the county were not involved, there might be some doubt in this respect. But there can be no doubt here. The vice which rendered the pledge contract illegal was the unauthorized discrimination undertaken to be effected in favor of the county against other depositors. These depositors will suffer loss as a result of the illegal contract, if the county be permitted to retain the notes. The possession of the notes by the county became injurious to these other depositors when the bank closed. Legal injury to the latter arose at that time. Relief from this injury can be obtained only through the banking commissioner. Plainly, then the banking commissioner, in the discharge of his duty in this respect, is entitled to recover the notes. The fact that a recovery of the notes by the banking commissioner will incidentally inure, to some extent, to the benefit of ordinary creditors whose rights are not infringed by the illegal transaction, cannot preclude such recovery. The county having no equities arising under the illegal contract, there are none to be adjusted."

In *Divide County v. Baird*, 212 N. W. 236, 244, the Supreme Court of North Dakota said:

> "This Court has adopted the view that the receiver of an insolvent bank, in addition to being an officer

of the court, represents the creditors (depositors) as well. We, and the courts generally, have distinctly recognized this dual aspect of the receiver's character. Nor are the interests of the depositors and of the corporation by any means wholly identical. Here a bank has illegally, in violation of positive statutes intended to protect depositors in banks, induced a county to violate another statute, also enacted in execution of the purpose to protect the interests of depositors, and secured a deposit of public funds by delivering a quantity of bills receivable as collateral; the county seeks to foreclose the pledge, with a double taint of illegality upon it, after the bank has become insolvent and is in the hands of a receiver to be wound up for the benefit of its creditors, who had nothing to do with the consummation of the unlawful scheme and were powerless to prevent it. The basis of the rule that the courts will leave the parties to an illegal contract where it finds them is that it will not aid or reward a wrongdoer. Here the depositors are guilty of no wrong; shall they be punished for the misdeeds of the guilty? When the wrong was done, they were powerless to speak or prevent it; now an officer of the court is charged with the duty of protecting their interests. Shall we say to him that there is no remedy whereby the innocent may be protected from the consequences of the unlawful conduct of the others? Section 22 of our Constitution provides that:

> 'The Courts shall be open, and every man for any injury done him . . . . shall have remedy by due process of law . . . . '

"And yet it is said that the court, after finding the injury, can only slap the defunct bank and the delinquent county on the wrist, and say to the depositors:

> 'We must leave you where we find you; we can do nothing, because the transaction was illegal,

and you have not returned something which, not you, but the bank got from the plaintiff.'

"To state the position ought to be sufficient to demonstrate its utterly untenable character. Such a holding would be a confession of judicial impotence to which the court is not prepared to subscribe. It would mean a notice to the people of this state that we are alike powerless to correct the wrongs which have been committed in the past and to prevent their repetition in the future. Once the parties are successful in executing their unlawful purpose, the victims of the legal fraud, although they are also the beneficiaries of the statutes which have been flouted, are helpless, and this court can do no more than convert itself into a debating society where legal theories may be expounded without practical or useful results. A tribunal without power to do justice is not a court of equity, but an academy. If we are powerless to give effect to the plainly expressed purpose of the Legislature to protect depositors, it is a usurpation to assume the name and put on the semblance of a court of equity."

Under the rule applicable to ultra vires contracts and those which are contrary to law, the party who has given up money may have Judgment for the return of the money, but he may not enforce his illegal contract.

In the present situation, the Railroad has a valid claim against the Receiver for the amount of its deposit with the Bank. This claim has been allowed. But the Railroad has no right to enforce a lien on the Liberty Bonds, because such lien in law has never existed.

II. Reply to Appellant's contentions:

Appellant quotes a general statement from *Scott v. Armstrong*, 146 U. S. 507, 36 Law Ed. 1062. We have no fault to find with such statement. The case is, however, not in point.

Appellant next quotes from *Brown v. Schleier,* 118 Fed. 981, 986-87. In that case, the Receiver for a national bank sought a recovery upon the theory that a lease which had been executed by a national bank was void, and that the Receiver would be entitled to recover back the consideration which had been paid in connection with the lease. The Circuit Court of Appeals correctly held that a national bank had a right to lease property upon which to transact its business and to construct a building upon such leased property. This was sufficient to have determined the case. The contention had been made that the bank had expended too much money in the construction of its building upon the leased premises. The Court said:

> "Another fact to be kept in mind is that the case in hand is not one where the bank assumed the exercise of a power which did not belong to it; but it is a case where, in the exercise of a power that was clearly conferred, it misused or abused it by making a greater expenditure for an authorized object than it ought to have made. Besides, the wrongful expenditure was made ten years before the present bill was filed. The building was completed in January, 1891, and the transaction at that time became an executed transaction."

In that case, the entire transaction had been fully completed on both sides many years before the Receiver was appointed. Moreover, while this case was affirmed by the Supreme Court[11] that Court disposed of the ultra vires feature of the case in the following language:

> "And, Appellant concedes 'that only the government may complain of an executed ultra vires conveyance of real estate to a corporation.' "

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11 Brown v. Schleier, 194 U. S. 18-25; 48 Law Ed. 857.

In other words, that Court merely stated counsel's own concession, that where a bank has acquired and paid for real estate before its insolvency, and the entire transaction has been closed on *both sides,* a Receiver could not thereafter set aside the transaction on the ground that the Bank had wrongfully acquired the property. In our case, the transaction has never been completed. The Texas and Pacific Railway Company is now seeking to have the illegal and void contract enforced, and to have the void lien foreclosed. This it cannot do.

Appellant then says:

> "Instead of applying the holding in the Pullman Car case, [12], this Court should apply to the case at bar the rule followed in most jurisdictions that 'an ultra vires transaction when executed by one of the parties may become enforceable by estoppel' (Corpus Juris, Vol. 14a, Sec. 2170, p. 324), which rule, Corpus Juris says, 'some of the lower federal courts,' evidently influenced by the rule of their local jurisdictions, have followed in holding that 'a party to an ultra vires transaction who has enjoyed the benefits thereof is estopped from denying its validity,' (C. J. Vol. 14a, Sec. 2170, pp. 325, 326)."

Appellant does not complete its quotation from Corpus Juris, Vol. 14a, page 325 (324). We give the full quotation:

> "Some of the lower Federal Courts have not been consistent in following the rule of the Supreme Court of the United States, and, evidently influenced by the rule of their local jurisdictions, have held that a party to an ultra vires transaction who has enjoyed the benefits thereof, is estopped from denying its validity."

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12 Central Transportation Company v. Pullman Palace Car Company, 139 U. S. 24, 48, 35 Law Ed. 55.

We also quote from Corpus Juris, Vol. 14a, page 319, Section 2169:

> "The doctrine of the Supreme Court of the United States, together with the English Courts, and some of the State Courts, is that no performance on either side can validate an ultra vires transaction or authorize an action to be maintained directly upon it."

Substantially the same statement is found in Corpus Juris, Vol. 14a, page 582, Section 2529.

In Corpus Juris, Vol. 14a, page 326, note (a), it is said:

> "One of the Federal Courts has taken the view that the rule followed by the Supreme Court applies only to quasi public corporations, and not to private corporations, *Bowman v. Foster, Etc., Hardware Company,* 94 Fed. 592, 597 (where it is said: 'I am aware that quasi public corporations—as, for instance, railroad corporations—which owe important duties to the public, are governed by a different rule. They will not be allowed to do any ultra vires act which, in effect, disqualifies them from discharging their duties to the public; and, if they do, they are not estopped to invoke the doctrines of ultra vires.')."

The business of banking is charged with a public interest. It is in the interest of the depositors and general creditors that a bank is prevented from pledging its assets to secure the payment of deposits except when specially authorized by Statute. This same public interest demands that the illegal lien be declared unenforceable.

A full reading of the cases heretofore cited on the question of estoppel will make the existence of this public interest clearly apparent.

Appellant cites the case of *Eastern Building and Loan*

Association v. Williamson, 189 U. S. 122, 47 Law Ed. 735. In the opening paragraph in that case, Mr. Justice Brewer said:

> "The Federal question presented arises on the contention that the South Carolina Courts did not give 'full faith and credit . . . .to the public acts, records and judicial proceedings' of the State of New York. . . ."

The learned Justice then quotes, from the decision of the Court of Appeals of New York, and says:

> "We deem it unnecessary to add any observations of our own to these satisfactory declarations of the *law of New York*."

Appellant also relies upon the case of *State Bank of Commerce v. Stone*, 184 N. E. 750 (N. Y. 1933). Here again, the Court merely states the New York doctrine, which is entirely different from the doctrine approved by this Court.

Corpus Juris, in Vol. 14a, at page 319, Section 2169, says:

> "The doctrine of the supreme court of the United States together with the English courts and some of the state courts is that no performance upon either side can validate an ultra vires transaction or authorize an action to be maintained directly upon it. However, the great weight of authority in the State courts is to the effect that a transaction which is merely ultra vires and not malum in se or malum prohibitum although it may be made by the state a basis for the forfeiture of the corporate charter or the dissolution of the corporation, is, if performed by one party, not void as between the parties to all intents and purposes, and that an action may be brought directly upon the transaction and relief had according to its terms."

Then follows a list of cases showing that New York is one of the states which does not follow the ruling of the Supreme Court with reference to the enforcement of ultra vires tracts.

Appellant also cites *Shornick v. Butler,* 185 N. E. 111. This is an Indiana case. In that state, as shown by the note in Corpus Juris, the New York rule is followed, not the rule of this Court.

Analagous to the question here presented would be a case such as we now state. In Texas, the head of a family may not give a valid mortgage upon his homestead except for purchase money and improvements. Suppose a case where, in violation of such law, a married man gives his note for $5000.00, secured by a mortgage on his home, and obtains from a banker the sum of $5000.00 on the faith of such note and mortgage. Concede that the banker, while knowing that the property is a homestead, believes that the mortgage is valid. Would anyone contend that the banker could not only sue and recover Judgment for the return of the money, but could also foreclose a lien on the homestead? The Court would certainly hold that a valid lien never existed, and could not be foreclosed.

We must remember that the Liberty Bonds here involved were never the property of The Texas and Pacific Railway Company.

They were at all times the property of the Bank.

The Bank did not receive these bonds by reason of the ultra vires contract.

The Receiver is unquestionably the owner of the bonds now.

The Texas and Pacific Railway Company is seeking to foreclose a lien upon the bonds. The lien is void.

The Court refused to foreclose the void lien, and declared the lien to be void.

If the Bank were solvent and if The Texas and Pacific Railway Company were suing the Bank for the amount of the deposit and asking Judgment for foreclosure of a lien on the Liberty Bonds, the Court would enter Judgment for the amount of the deposit, but would deny the prayer for a foreclosure of a lien on the Bonds, because no lien in law ever existed.

So, in this case, Appellant has Judgment for the amount of its deposit, but it is denied its prayer for a foreclosure of lien.

C. NO BASIS EXISTS FOR GRANTING THE TEXAS AND PACIFIC RAILWAY COMPANY A PREFERRED CLAIM AGAINST THE RECEIVER FOR THE AMOUNT OF ITS DEPOSIT BALANCE.

Argument

This Court is, of course, familiar with the proof that must be made in order to obtain a preference.

It must be shown that the deposit was made with the understanding that the funds deposited should be held in trust and not used by the bank in its business as its own funds. Here, the evidence clearly indicates that the parties intended that the deposited funds should be used by the bank in its business, and that a debtor and creditor relation should exist.

Since the parties intended that the deposited funds should be used by the bank as its funds, no presumption

arose to the effect that the deposited funds would be kept in the possession of the bank.

In the second place, in order to establish a preference, is must be shown that new money, in cash, came into the possession of the bank, as a result of the particular transaction, and that such money remained in the possession of the bank until insolvency, and was then delivered over to the Receiver.

In this case, there is no proof to show that after January 29, 1931, new money, in cash, came into the bank from The Texas and Pacific Railway Company.

No proof was offered to show whether, after January 29, 1931, the bank had any cash in its vaults.

No showing was made as to the amount of cash on hand when the bank became insolvent.

It does not appear how much, if any, cash passed into the possession of the Receiver. There is no proof that the assets delivered to the Receiver were augmented by any deposits made by The Texas and Pacific Railway Company.

No fund or property in the hands of the Receiver is shown to be impressed with a trust in favor of The Texas and Pacific Railway Company.

There was no basis, either in the pleadings of the Railroad Company or in the evidence introduced, to justify the allowance of a preference.

A few of the authorities which sustain the propositions above stated are: *Schuyler v. Littlefield,* 232 U. S. 707; *Blakely v. Brinson,* 286 U. S. 254; *Keyes v. Paducah and*

Illinois R. R. Co. 61 Fed. (2d) 611; *Empire State Surety Co. v. Carroll County*, 194 Fed. 593, 604; *Frelingheusen v. Nugent*, 36 Fed. 229, 239; *American Can Company v. Williams*, 178 Fed. 420, 422, 423; *Board of Commissioners v. Strawn*, 157 Fed. 49, 54; *Larabee Flour Mills v. First National Bank*, 13 Fed. (2d) 330, 331; *Dudley v. Richards*, 18 Fed. (2d) 876, 878; and *In Re Brown*, 193 Fed. 24, 29.

Respectfully submitted,

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APPENDIX

December 13, 1929.

Mr. Lewis E. Smith,
Grand Secretary,
Grand Lodge A. F. & A. M. of Nebraska,
401 Masonic Temple,
Omaha, Nebraska.

Dear sir:

Your letter of December 7 is received, stating that the Grand Lodge A. F. & A. M. of Nebraska has for several years carried a balance with a national bank, that this deposit has been secured by the bank depositing with the proper officers of the Grand Lodge Liberty bonds and Treasury certificates, and requesting to be advised whether it is legal for a national bank to secure a deposit of this sort in this manner.

There is no provision in the national banking laws expressly prohibiting the securing of deposits, but inasmuch as Congress has recognized the fact that the deposits of Federal moneys should be secured (Section 5153, U. S. R. S.), this office has always held that a national bank may pledge its assets to secure public deposits made subsequent to the pledge thereof. However, it is not believed that a national bank may pledge any of its assets to secure private deposits.

Respectfully,

(Signed) F. G. AWALT,
Deputy Comptroller.

APPENDIX

January 30, 1931.

President,
First National Bank,
Hornell, New York,

Dear sir:

Your letter of January 26 is received, stating that you have recently pledged certain of your securities for the purpose of securing a deposit placed with your bank by one of your correspondent banks; that Examiner O'Connor has informed you that according to Federal legislation passed sometime in the early part of 1930 national banks are prohibited from pledging any of their assets to secure deposits other than New York State deposits and postal savings, and requesting to be advised in regard thereto, and to be furnished a specific citation of the section of law covering this point.

The Act of June 25, 1930, amending Section 5153, U. S. R. S., expressly provides that:

> "Any association may, upon the deposit with it of public money of a state of any political subdivision thereof, give security for the safe keeping and prompt payment of the money so deposited, of the same kind as is authorized by the law of the State in which such association is located in the case of other banking institutions in the state."

The position of this office is that a national bank may not pledge any of its assets to secure individual deposits.

Respectfully,
(Signed) F. G. AWALT,
Deputy Comptroller.

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DEC 6 1933

CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1933.

No. 128.

THE TEXAS AND PACIFIC RAILWAY COMPANY, *Appellant*,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas, *Appellee*.

SUPPLEMENTAL REPLY BRIEF ON BEHALF OF S. O. POTTORFF, RECEIVER OF THE FIRST NATIONAL BANK OF EL PASO, TEXAS.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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We have shown that a pledge to protect a private depositor is illegal since it violates the policy of the law giving equal protection to all depositors. But, unless the enforcement of the pledge in this case is denied, that policy will be rendered nugatory. In other words, the present case is an example of those where a transaction fails because of public policy, and where that same public policy requires affirmative relief.

"Although the parties are in *pari delicto*, yet the court may interfere and grant relief at the suit of one of them,

where public policy requires its intervention, even though the result may be that a benefit will be derived by a plaintiff who is in equal guilt with defendant. But here the guilt of the parties is not considered as equal to the higher right of the public, and the guilty party to whom the relief is granted is simply the instrument by which the public is served." 13 Corpus Juris 497, Sec. 441.

The converse case of a bank being permitted to enforce an illegal agreement, because the public policy declaring the illegality requires the agreement to be enforced, is thus discussed by Professor Williston:

> "In some cases, where a refusal to enforce an agreement would produce the very effect which the law seeks to guard against, a corporation is allowed to enforce it, although it was particularly prohibited and made illegal. Thus, for the security of depositors and others, banks are prohibited from entering into certain kinds of loans or purchases. When a contract of this sort has been entered into, however, should the corporation be refused a right of recovery, the result would be the impairment of the assets of the bank—the very result which the law seeks to prevent, and, therefore, the bank is allowed to recover."

Williston on Contracts, sec. 1632, p. 2870, and cases cited. A defendant is not permitted to plead the illegal contract of a bank, where the enforcement of the contract is for the benefit of the bank. Thus, in Union Gold Mining Co. v. Nat'l Bank, 96 U. S. 640 (1877), Hunt, J., said that a defendant could not assert the *ultra vires* since "this would be to injure the interests of creditors, stockholders and all who have an interest in the safety and prosperity of the bank." So in Union Nat'l Bank of St. Louis v. Matthews, 98 U. S. 621 (1878), Swayne, J., said: "We cannot believe it was meant that stockholders, and perhaps depositors and other creditors, should be punished and the borrower rewarded, by giving success to this defence whenever the offensive fact shall occur."

The pledge in question was void and the bank itself could have rescinded the contract at any time. Not only *could* the bank have done this, but it *should* have done so. In Thomas v. West Jersey Railroad Co., 101 U. S. 71 on page 86, Miller, J., says:

> "Not only so, but it is a contract forbidden by public policy and beyond the power of the defendants to make. Having entered into the agreement, it was the duty of the Company to rescind or abandon it at the earliest moment. This duty was independent of the clause in the contract which gave them the right to do it. Though they delayed its performance for several years, it was, nevertheless, a rightful act when it was done. Can this performance of a legal duty, a duty both to stockholders of the Company and to the public, give to plaintiffs a right of action? Can they found such a right on an agreement void for want of corporate authority and forbidden by the policy of the law? To hold that they can, is, in our opinion, to hold that any act performed in executing a void contract makes all its parts valid, and that the more that is done under a contract forbidden by law, the stronger is the claim to its enforcement by the courts."

This would seem to end the matter. If the bank itself could and should have rescinded the pledge, then the receiver is justified in doing so on behalf of the bank and of the depositors.

Appellants urge that the pledge in question was executed on both sides and therefore the transaction is unassailable. The argument is unsound, since the pledge contemplated, not so much the deposit of securities, as the sale in case of default, and it is the sale which the railroad is now trying to compel. That the sale is the execution of the agreement is decided by the Supreme Court in First National Bank of Xenia v. Stewart, 107 U. S. 676, in which the court, speaking of an *ultra vires* pledge of bank stock by a borrower from a bank, says:

"While this section, in terms, prohibits a banking association from making a loan upon the security of shares of its own stock, it imposes no penalty, either upon the bank or borrower, if a loan upon such security be made. If, therefore, the prohibition can be urged against the validity of the transaction by anyone except the government, it can only be done before the contract is executed, while the security is still subsisting in the hands of the bank. It can then, if at all, be invoked to restrain or defeat the enforcement of the security. When the contract has been executed, the security sold, and the proceeds applied to the payment of the debt, the courts will not interfere with the matter."

Instead of the case at bar involving an executed transaction, it would seem that the transaction in question is entirely executory; and this court recognizes that such transactions are void and unenforceable.

Respectfully submitted,

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FILE COPY

FILED
SEP 25 1933
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1933.

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Petitioner,
v.
S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,
Respondent.

No. 128.

BRIEF ON BEHALF OF ILLINOIS CENTRAL RAILROAD COMPANY.

CHARLES N. BURCH,
EDWARD W. SMITH,
Amici Curiae.

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No. 128.

BRIEF ON BEHALF OF ILLINOIS CENTRAL RAILROAD COMPANY.

May It Please the Court:

This brief is filed in pursuance of the following personally signed stipulation filed in this cause:

"STIPULATION.

"The parties to the above entitled and numbered cause, and their counsel, hereby consent to the filing of an amicus curiae petition and/or brief in this cause by Charles N. Burch and Edward W. Smith on behalf of the Illinois Central Railroad Company.

"Dated this 2nd day of September, 1933.

S. N. Russell,
Del W. Harrington,
T. D. Gresham,
M. E. Clinton,
Counsel for Petitioner.
Thornton Hardie,
Counsel for Respondent."

The questions discussed herein are:

(1) May a national bank make a valid pledge of part of its assets to secure the deposit of a private depositor, and

(2) Even though such pledge be invalid, may the receiver of a national bank recover the pledged assets without returning to the depositor his deposits?

The Illinois Central Railroad Company is deeply interested in the result of this litigation, for the reason that the same questions involved herein are likewise involved in the case of *Illinois Central Railroad Company vs. A. F. Rawlings, Receiver of Planters National Bank of Clarksdale, Mississippi* (recently decided by the United States Circuit Court of Appeals for the 5th Circuit, but not yet officially reported), and the Illinois Central Railroad Company is now engaged in the preparation of a petition for certiorari which will shortly be filed in this court for the purpose of seeking a review of the decision of the United States Circuit Court of Appeals in the said Rawlings case. The decision of the Circuit Court of Appeals in the Rawlings case is the same in substance and effect as the decision of said court in the instant Texas and Pacific case.

We fully approve the petition for certiorari and brief in support thereof which has been filed by the Texas & Pacific Railway Company in this cause, and in view of the conflict of opinion in lower federal courts, as well as the conflict of opinion in state courts, and the importance of the questions involved, it is respectfully submitted that this court should grant the petition for certiorari herein.

This conflict of opinion was pointedly referred to by the Circuit Court of Appeals for the 7th Circuit in *Sneeden v. City of Marion,* 64 Fed. (2) 721, in the following language:

> "The courts in this country are not in accord as to whether national or state banks may pledge their assets as security for deposits of public or private money. This diversity of opinion has arisen by reason of the difference of state statutes, and a contrariety of economic views in applying the Federal statute and in formulating state policies." (p. 722.)

The Circuit Court of Appeals for the 4th Circuit in *Schumacher v. Eastern Bank & Trust Company,* 52 Fed. (2) 927, said:

> "Whether a bank may pledge its assets for the security of an ordinary deposit is a question as to which there is conflict of authority. For cases denying such power, see Smith v. B. & O. R. Co. (D. C.), 48 Fed. (2) 861, Divide County v. Baird, Receiver, 55 N. D. 45, 212 N. W. 236, 51 A. L. R. 296; Farmers' & Merchants' State Bank v. Consolidated School District, 174 Minn. 286, 219 N. W. 163, 65 A. L. R. 1407. For cases asserting it, see Ward v. Johnson, 95 Ill. 215; Ahl v. Rhoads, 84 Pa. 319; Cameron v. Christy, 286 Pa. 405, 133 A. 551; Richards v. Osceola Bank, 79 Iowa 707, 45 N. W. 294; McFerson v. National Surety Co., 72 Colo. 482, 212 P. 489; Ex parte Grand Lodge, G. U. O. O. F. (State ex rel. Bradley v. People's Federation Bank), 147 S. C. 103, 144 S. E. 841; Williams v. Hall, 30 Ariz. 581, 249 P. 755; Grigsby v. People's Bank, 158 Tenn. 182, 11 S. W. (2d) 673. And as bearing on the question generally, see notes

in 51 A. L. R. 313, and 65 A. L. R. 1412. Although some of the cases draw a distinction between a pledge of assets to secure a deposit of public funds and a pledge to secure a private deposit, there would seem to be, in the absence of statute, *no valid basis for such distinction;* and this court has expressly upheld a pledge of assets by a national bank to secure a deposit of funds. Burrowes v. Nimocks, supra."

HAS A SOLVENT NATIONAL BANK THE POWER TO PLEDGE PART OF ITS ASSETS TO SECURE THE DEPOSITS OF A RAILROAD COMPANY, SUCH PLEDGE AGREEMENT BEING ENTERED INTO IN GOOD FAITH BY THE PARTIES THERETO?

The powers of national banks are set out in 12 United States Code Annotated, Sec. 24 (R. S., Sec. 5136) et seq. Among the powers conferred are:

"Third. To make contracts." and * * *.

"Seventh. To exercise by its board of directors, or duly authorized officers or agents, subject to law, *all such incidental powers as shall be necessary to carry on the business of banking;* by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; *by receiving deposits;* by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this chapter.

"But no association shall transact any business except such as is incidental and necessarily preliminary to its organization, until it has been authorized by the Comptroller of the Currency to commence the

business of banking. (R. S., Sec. 5136; July 1, 1922, c. 257, Sec. 1, 42 Stat. 767.)"

It will thus be seen that national banks are given the broad power of making contracts and "all such incidental powers as shall be necessary to carry on the business of banking * * * by receiving deposits."

The natural and obvious construction of this language is that as the bank is given power of receiving deposits, it may prescribe the terms and conditions under which said deposits are received and may make contracts looking to the safety or security of such deposits. The powers granted are broad and general and properly so, as Congress plainly intended to leave to the judgment and discretion of the officers of such banks the manner in which deposits would be received and the conditions under which they would be received, subject, however, to the supervision of the Comptroller of the Currency.

And so it is, as the court judicially knows, that some banks will accept a deposit account only in excess of a certain amount, the amount varying in different banks; some banks pay interest on checking deposits and some banks do not; some banks receive deposits only during certain hours of the day and other banks observe different hours. As to all such matters we assume that it will not be denied that national banks may exercise their own judgment and discretion.

Ordinarily banks seek and desire to retain deposits, as deposits represent a large part of the capital upon which banks operate, and generally this capital is furnished by depositors without the payment of any interest by the banks.

There is nothing immoral in a bank pledging its assets to secure deposits. There is no statute prohibiting such pledging. What has been done is neither *malum in se* nor *malum prohibitum*. As said by the Supreme Court of Indiana in the recent case of *Schornick v. Butler*, 185 N. E. 111:

> "We find no constitutional or statutory enactments, no practices of officials, or judicial decisions in this state indicating that the pledging of collateral to secure deposits is against public policy. *There is nothing inherently wrong or immoral in such a transaction.*"

There is no federal statute prohibiting a national bank from pledging its assets to secure a private depositor, nor is there any rule or regulation or order issued by the Comptroller of the Currency to prohibit such pledging. If there had been such a rule or regulation it would certainly have been produced by the receiver. We are dealing, therefore, with an act which is neither immoral nor inherently wrong. On the other hand, it is a highly commendable act for a railroad company, which owes the duty to the public of honest and efficient management and operation, to make every proper effort to conserve its revenues so that the public may be properly served.

As indicating the view which Congress takes of the pledging of assets to secure deposits, it is to be noted that Congress puts the imperative duty upon the Secretary of the Treasury to require national banks "to give satisfactory security" for the safekeeping of public money of the United States. (12 United States Code Annotated, Sec. 90.)

It must therefore be accepted as settled that there is nothing wrong from a moral standpoint and nothing in violation of any statute in the pledging of assets to secure deposits, but on the other hand such a practice (certainly so far as public money is concerned) has the positive approval of Congress.

We are here in a court of equity and are stressing the importance of the character of the act which has been done in order to bring clearly to the attention of the court the fact that the depositor (Texas & Pacific Railway Company) is in court with clean hands and entitled to relief unless such relief is forbidden by some positive rule of public policy, not yet legislatively announced by Congress or judicially announced by this court.

The court below, however, in this case proceeded on the theory that national banks had not been granted the power to pledge their assets to secure private depositors and hence, the power not having been granted, did not exist and therefore the pledge agreement is invalid. The court below held specifically that the bank "had no such power" and pointedly rejects the proposition that "the giving of pledges for private deposits is a reasonable incident to the business of receiving deposits and necessary to the proper conduct of the business of a national bank."

As we have already seen, national banks are given "all such incidental powers as shall be necessary to carry on the business of banking" * * * "by receiving deposits." National banks have been in existence since the Act of Congress of June [illegible] 1864, a period of sixty-nine years. The numerous decisions of state and federal courts dis-

cussing the validity of pledges to secure deposits, whether public or private, show that the practice of pledging assets to secure deposits is a well known one, and one that has been in existence for many years.

In a recent opinion the Supreme Court of Tennessee said, relative to the practice of giving security for deposits:

> "It is a practice followed by many banks. We are unable to draw any substantial distinction between transactions where a bank borrows money for a specified time, or receives it on deposit for a stated period, or receives it on deposit subject to check. *In either case the relationship is the same—debtor and creditor*—the bank receives and uses the money of the creditor, to its profit, on a promise to repay.
>
> "As was stated in *Trust Co. v. Rose,* supra, it is for the *legislature* to say whether a sound public policy forbids such a transaction as this record presents."
>
> Grigsby v. The People's Bank, 158 Tenn. 193.

With utmost deference to the opinion of the court below, it is respectfully submitted that whether the pledging of assets to secure deposits is one of the "incidental powers" granted to national banks and whether such power is "necessary to carry on the business of banking" is one which the Comptroller of the Currency, with his expert knowledge of the subject of banking, is in a better position to determine than are the courts, and the fact that the practice has been in vogue for many years and has not been prohibited by any Act of Congress or by any general order of the Comptroller of the Currency is in and of

itself an expression by Congress and the Comptroller that the practice is a proper one, even though, in individual instances as to particular pledges, the Comptroller may have "scolded" or disapproved. As stated by Judge Dickinson in his dissenting opinion in *B. & O. R. Co. v. Smith,* 56 Fed. (2) 799: "Actions speak louder than words." It is inconceivable that the Comptrollers of the Currency during a period of sixty-nine years, having knowledge of the practice, would not have issued a general order forbidding same if the practice were wrong in principle. Said Judge Dickinson (p. 804):

> "We are not as much impressed by the opinions of individual comptrollers as the majority of the court has been. We grant the rule of construction that when the executive has construed an act of Congress in order to carry it into effect that the courts will not lightly change the executive interpretation of the meaning of the act. It may be and usually is disrupting to so do. There has, however, been no such executive or administrative construction given to this act. The practice has of late grown up, and recent happenings in banking circles has doubtless furthered it for depositors, particularly those carrying large balances such as railroads, trustees for estates, and banking institutions to ask for and receive security for their deposits. Comptrollers have known of this. Some of them have doubtless scolded; but they have permitted it, and one or two of them have publicly announced their disapproval of the practice. Actions speak louder than words. All disruption there may be, will result from the ruling that the banks are without the power to do this."

It is also a fair assumption that Congress itself would have prohibited such a general practice by express statutory prohibition if the practice were wrong in principle or detrimental to public interests.

A FAIR CONSTRUCTION OF THE ACTS OF CONGRESS INDICATES THAT IT HAS ALWAYS BEEN ASSUMED THAT NATIONAL BANKS HAVE THE POWER TO PLEDGE SECURITIES TO SECURE PRIVATE DEPOSITS.

An examination of the legislation of Congress will show that national banks have the power to secure deposits, whether public or private.

As already shown, there is first granted in broad terms and without restriction "all such incidental powers as shall be necessary to carry on the business of banking" * * * "by receiving deposits": Later, however, in the same legislation the attention of Congress was directly challenged as to the security of deposits and, by Section 90 of 12 United States Code Annotated, relative to national banking associations, it is provided:

> "The Secretary of the Treasury *shall* require the associations thus designated to give satisfactory security, by the deposit of United States bonds and otherwise, for the safekeeping and prompt payment of the public money deposited with them."

By *requiring* security for public money deposited in banks, Congress necessarily assumed that national banks had the power to give security, to be exercised at the option of such banks, and, assuming that national banks already had such power, Congress merely took away the

option of such banks as to giving security and mandatorily required that such security should be given for public money of the United States. We respectfully submit that the requirement that such security shall be given, inevitably implies the premise that the power to give security already existed, and so it is in other Acts of Congress relative to various kinds of public money, Congress, assuming that the power to give security already existed, mandatorily required that security shall be given.

A reference to the other acts are set out in the margin.*

In Section 24, giving national banks "all such incidental powers as shall be necessary to carry on the business of banking * * * by receiving deposits," the word "deposits" is simply used. The expression is not private deposits or public deposits but the word "deposits" includes all kinds of deposits whether public or private or semi-public or semi-private.

Congress, therefore, knowing that banks receive both private and public deposits and having had its attention challenged to security for deposits, plainly intended by its legislation that, so far as public deposits of the Govern-

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*As to receivership moneys, 39 Stat. 121, 12 USCA Sec. 192; as to making land and joint stock banks depositories, 39 Stat. 365, 12 USCA Sec. 701; as to postal service funds, 39 Stat. 159, 39 USCA Sec. 759; as to depositories of public moneys, 45 Stat. 492, 12 USCA Sec. 332; as to Indian moneys, 36 Stat. 1070, 25 USCA Sec. 156, and 40 Stat. 591, 25 USCA Sec. 162; as to the deposit of money received from the sale of United States bonds, 40 Stat. 504, 31 USCA Sec. 771.

ment are concerned, security *must* be given, but so far as private deposits are concerned the giving of security was left to the determination and judgment of individual banks acting under the jurisdiction and supervision of the Comptroller of the Currency.

The construction for which we are contending is supported by the Attorney General of the United States, for in (1915) 30 Op. Atty. Gen. 341, it was said relative to Sec. 90 of 12 USCA:

> "It is believed that this section is more reasonably construed *as a recognition of the existence of the power on the part of national banks to give security for deposits* than as a grant by implication of authority to give security for *Government deposits alone.*"

We submit, therefore, that the right of national banks to give security for private deposits has been assumed by Congress since 1864 and similarly assumed by the Attorneys General and by the Comptrollers of the Currency for the same period.

We now come, however, to an amendment of Section 90 of 12 United States Code Annotated, said amendment being the Act of June 25, 1930, reading as follows:

> "Any association *may,* upon the deposit with it of public money of a *State or any political subdivision thereof,* give security for the safe-keeping and prompt payment of the money so deposited, of the same kind as is authorized by the law of the State in which such association is located in the case of other banking institutions in the State. (As amended June 25, 1930, c. 604, 46 Stat. 809.)"

As will be seen, this amendment has reference, not to the public money of the United States but to the public money "of a state or any political subdivision thereof."

The statement of this amendment is not that security shall be given but security *may* be given and it is therefore contended by the Receiver that as the act only grants authority to give security for the public moneys of a state or political subdivision thereof, therefore, it was the plain intention of Congress to withhold the power to give security for a private deposit. This is a plain *non sequitur* for the following reasons: in the first place, it was known that national banks did give security to private depositors and if Congress had intended to stop such practice it would have been prohibited by express enactment; second, the history of the passage of this Act of 1930 shows that it was passed merely to quiet doubts of some timid national bankers and to confirm in direct and positive statutory form a power (though already existing) to national banks so that they could compete with state banks, which were obtaining state deposits by giving security therefor.

The history of this legislation is thus set out in *B. & O. v. Smith*, 56 Fed. (2) 802:

> "In Senate Report No. 67, 71st Cong. 2nd Sess., the committee based its favorable report upon a letter from the Attorney General of Minnesota, reading in part as follows: 'The United States district court for this district has held that it may not thus pledge its assets to secure private deposits and the trend of authority generally seems to be to the effect that a bank may not in any case pledge its assets to secure a deposit unless authorized by law so to do. The

national banks of this State have pledged with the State and the various subdivisions thereof millions of dollars in Government and other bonds as security for public deposits. They are anxious to be permitted to do so, and we are willing that they should. Under the law as it now stands we may be taking a chance in accepting such pledges from the national banks, and we should like to have the chance removed by legislation in Congress which will specifically authorize such pledges by national banks.' ".

"From House Report No. 1657, 71st Cong. 2d Sess., it appears that the committee reported favorably upon the bill (S. 486) because of a request from the Acting Secretary of the Treasury, reading in part as follows: 'While the office of the Comptroller of the Currency has consistently taken the position that national banks *have the right to give security for the safe-keeping and prompt payment of public moneys of the State or political subdivision thereof deposited with such national banking associations,* several recent decisions have thrown some doubt on this question with the result that in some States the State banks may secure the public deposits, but the officers of the State are in doubt about depositing with the national banks in the absence of any specific law by Congress on the subject. It would be extremely helpful, therefore, if it is possible for your committee to report out, and the House pass, S. 486.' "

From this it appears that the Comptrollers of the Currency have always assumed and taken the position that national banks have the right to give security for state funds, county funds and municipal funds. Such assump-

tion is correct and is necessarily based upon the proposition that the original power given of carrying on a banking business "by accepting deposits," clearly included the power to give security for deposits, whether such deposits were public funds of the United States, public funds of a state, county or city, or private funds of a private depositor. The Comptroller of the Currency could not consistently and logically assume that national banks had the power to give security for the funds of a municipality unless at the same time he necessarily assumed that there was similar power to give security for the deposits of a private depositor. The one assumption accompanies the other assumption and, as said by the Attorney General of the United States in 30 Op. Atty. Gen. 341, quoted above, the recognition of the existence of the power on the part of national banks to give security for deposits is not to be confined to "government deposits *alone.*"

In view, therefore, of the long practice of giving security for private deposits and in view of the history of the passage of the amendatory act of 1930, it cannot be doubted that the power to give security for private deposits has always been a power which national banks have had, and there is no room for the application of the doctrine of *expressio unius exclusio alterius.* As said by Judge Dickinson in his dissenting opinion in *B. & O. v. Smith,* supra:

> "It is true that there are now acts which expressly confer authority to secure public deposits but none to secure private deposits. *The genesis of such acts* takes away all significance which they might otherwise have in respect to the question under discussion.

> Some official was concerned over the deposit of public moneys for which he was responsible. He asked for relief and Congress gave it to him without concerning itself with the effect of the legislation upon others. Legislatures not infrequently do this. Had these provisions been part of the original act which conferred the power, they would have great significance. If, however (as we think is true), the original act gave the power, the question becomes, not whether the subsequent legislation confers it, but whether it takes away a power before given. We suppose no one would urge that it does."

Likewise, Judge Alschuler in his dissenting opinion in *Sneeden v. City of Marion,* 64 Fed. (2), page 732, said:

> "The act was calculated to remove any doubt of the right of the national banks to be on the same footing as the state banks of the several states."

In view therefore of the history of the passage of the Act of June 25, 1930, amending Section 90 of 12 U. S. C. A., it is perfectly clear that the object of said act was to put in clear, positive and statutory form a power already existing, so that national banks, in their competition with state banks for state deposits, might be able to refer to a positive statute conferring power to give security for state deposits, rather than relying upon the general power, already existing, as set out in general terms in Section 24 of 12 U. S. C. A.

The whole object of the legislation was to aid national banks in their competition with state banks for deposits. At the time of the passage of this act of 1930, Congress

knew that national banks had private deposits as well as public deposits and while it was on the subject of security for deposits, Congress, if it had intended to prohibit security for private deposits, would certainly have said so, as Congress must be presumed to have known that the practice of giving security for private deposits had been in effect for many years.

THE MEANING OF THE WORD "NECESSARY."

In Section 24 of 12 U. S. C. A., national banks are given "all such incidental powers as shall be necessary to carry on the business of banking" * * * "by receiving deposits."

Plainly the word "necessary" is not intended to mean elemental or rudimentary wants. Plainly it is intended to mean reasonably necessary, useful or convenient. In order to receive deposits a national bank need not own its own building, it can rent a building, yet we assume no one would contend that it had no power to own a building because ownership was not absolutely necessary for the receiving of deposits and transacting other banking business, whereas renting a building would do just as well. (Sec. 29 of 12 U. S. C. A.) Likewise deposits could be received in a plain, unornamented building, but we suppose no one would contend that a national bank does not have the power to have marble counters, tile floors, and nickel-plated cages merely because less ornamental surroundings would be sufficient for the receiving of deposits.

We think the construction which Chief Justice Marshall gave to the word "necessary" in *McCullough v. Maryland*, 4 Wheaton 316, 4 L. Ed. 579, is final on this subject.

Said he (referring to the meaning of the word "necessary" as used in Sec. 8, Art. 1 of the Constitution):

> "If reference be had to its use, in the common affairs of the world, or in approved authors, we find that it frequently imports no more than that one thing is *convenient,* or *useful,* or essential to another."

The meaning of "necessary" in this connection has already been so fully discussed in the brief filed by the Texas & Pacific Railway Company that we forbear from further discussion.

A BANK GIVING SECURITY FOR DEPOSITS NOT DISTINGUISHABLE IN PRINCIPLE FROM A BANK BORROWING MONEY ON A DEMAND NOTE SECURED BY COLLATERAL OF THE BANK.

Concededly a national bank has power to borrow money on a demand note and to secure the loan by the pledging of collateral of the bank, but such transaction is in no way different in principle from pledging collateral to secure a deposit. Both transactions create the simple relation of debtor and creditor. As said by this court in *Auten v. United States National Bank of New York,* 174 U. S. 142:

> "The very first banking in England was pure borrowing. It consisted in receiving money in exchange for which promissory notes were given payable to bearer on demand, and so essentially was this banking as then understood, that the monopoly given to the Bank of England was secured by prohibiting any partnership of more than six persons 'to borrow,

owe, or take up any sum or sums of money on their bills or notes payable at demand.' And it had effect until 1772 (about thirty years), when the monopoly was evaded by the introduction of the deposit system. The relations created are the same as those created by the issue of notes. In both a debt is created—the evidence only is different. In one case it is a credit on the banker's books; in the other his written promise to pay. In the one case he discharges it by paying the orders (checks) of his creditor; in the other by redeeming his promises. These are the only differences.''

ASSUMING THE PLEDGE OF ASSETS TO SECURE A PRIVATE DEPOSITOR IS INVALID, THAT IS, ULTRA VIRES, MAY THE RECEIVER OF THE NATIONAL BANK HOLD THE DEPOSITS OBTAINED BY VIRTUE OF THE PLEDGE AND STILL, AT THE SAME TIME, REQUIRE A RETURN OF THE PLEDGED ASSETS TO HIM?

The record herein is clear that the deposits would not have been made by the Railway Company unless security had been given by the bank. The record is also clear that at the time the deposits were made the bank was solvent and the pledge agreement was made in good faith. It seems plainly inequitable on its face that the receiver of a national bank may hold both the deposits of the railway company and also require the return to him of the pledged assets. However, the United States Circuit Court of Appeals for the Third Circuit has so held by a divided court in *B. & O. v. Smith,* 56 Fed. (2) 799, and likewise the Circuit Court of Appeals for the 5th Circuit has so held in the instant case of *Texas & Pacific Railway Com-*

pany v. Pottorff, 63 Fed. (2) 1, and in the case of *Illinois Central Railroad Company v. Rawlings, Receiver* (not yet officially reported).

It is respectfully submitted that these decisions are in conflict with the decisions of this court and with the opinion of the United States Circuit Court of Appeals for the 4th Circuit in *Schumacher v. Eastern Bank & Trust Company*, 52 Fed. (2) 925.

In the Schumacher case just referred to there were advances made by the Eastern Bank & Trust Company of Newbern, N. C., to the First National Bank at Newbern, N. C., the national bank assigning and pledging certain of its assets to secure such advances. The court discusses at some length whether these advances were to be considered as loans made by the trust company to the national bank or as deposits made by the trust company in the national bank. However, either situation constituted the relation of debtor and creditor and the question was, even though the national bank may have exceeded its powers and even though the trust company may have exceeded its powers, did the receiver of the national bank have the right to hold both the money advanced and at the same time insist on the return of the assets pledged to secure this advance? This question was answered in the negative. In the course of the opinion the court said:

> "Of course, a pledge of assets in contemplation of insolvency for the sake of creating a preference is avoided by section 5242 of the Revised Statutes (12 USCA Sec. 91); but, in the absence of a preferential transfer in contemplation of insolvency, there is no

federal statute under which a pledge of assets as security for a loan or *deposit* may be avoided. See Paton's Digest of Banking Law (1926), Vol. 1, Sec. 641."

And:

"But at all events, we must decide the question presented on the basis of the inherent nature of the transactions, and not with reference to their form. Neither the fact that the trust company exceeded its legal limit of loans, nor that the bank sought to avoid showing an increase of bills payable, would have authorized the bank to retake the securities it had pledged for the repayment of the money borrowed (Nat. Bank v. Matthews, 98 U. S. 621, 25 L. Ed. 188; 7 C. J. 713 and cases cited); and it is well settled that, where there is no preferential transfer in contemplation of insolvency, *the receiver has no greater right in securities pledged than the bank itself would have had.* See Burrowes v. Nimocks, supra, and cases there cited."

Schumacher v. Eastern Bank & Trust Co., 52 Fed. (2) 925.

In *Union National Bank v. Matthews*, 98 U. S. 621, there was drawn in question the power of a national bank to take as collateral security for a note another note which was secured by a deed of trust on real estate. The question was one of the powers of the bank under the national banking laws now under consideration. In that case the court said:

"A court of equity is always reluctant in the last degree to make a decree which will effect a forfeiture.

> The Bank parted with its money in good faith. Its garments are unspotted. Under these circumstances, *the defense of ultra vires,* if it can be made, does not address itself favorably to the mind of the Chancellor."

And in the same case the court quoted with approval the following from Sedgwick on Statutory and Constitutional Construction:

> "Where it is a simple question of authority to contract, arising either on a question of regularity of organization *or of power conferred by the charter, a party who has had the benefit of the agreement cannot be permitted in an action founded upon it to question its validity.* It would be in the highest degree inequitable and unjust to permit a defendant to repudiate a contract, the benefit of which he retains."

The same equitable principle is expressed by Chief Justice Marshall as to a party attempting to claim both under and against a will:

> "It is the maxim in a court of equity not to permit the same person to hold *under and against a will.*" *Herbert v. Wren,* 7 Cranch, 378.

In the case at bar the effect of the decision of the Circuit Court of Appeals is to allow the receiver of the bank to retain the benefits of the pledge contract (that is, the deposits) and at the same time to repudiate the pledge of the bank to secure said deposits. This feature of the case has already been so fully discussed in the brief filed by the Texas & Pacific Railway Company that we will close this brief by referring to two recent deci-

sions of state courts of the highest respectability and authority.

In the recent case of *State Bank of Commerce v. Stone*, 261 N. Y. 175, 184 N. E. 750, the Court of Appeals of New York, after holding that the state bank there involved had no implied powers under the laws of New York to pledge assets for security for private deposits, yet at the same time held that a corporation cannot retain what it has received under an ultra vires contract and at the same time refuse to perform the contract. In the case under discussion the bank had become insolvent and suit was brought by the Superintendent of Banks to recover the pledged assets. In disposing of the case the New York court said:

> "This leads to the conclusion that the agreement made by the State Bank of Commerce of Brockport, N. Y., with the defendant, and the pledge of $15,000 in bonds to secure a $5,000 deposit, was contrary to law and beyond the power and authority vested in the officers of the bank.
>
> "This does not necessarily mean, however, that the judgment of the courts below must be reversed, as we have to consider the effect of *ultra vires*. In pledging these bonds, the officers were acting for and on behalf of the bank, and for its business, apparently seeking to obtain deposits which, under the Bank Law, it was authorized to receive. They applied the deposits to the bank's business, and the bank has had and received the benefit of the money due to the agreement which the bank made, and the bonds which it delivered as security. Under these circumstances, it would not be just for the bank or its creditors to

accept all the benefits and repudiate the burdens, unless the acts of the bank be in violation of some direct and positive statute. Whatever the difference of view there may be as to the effect of ultra vires on corporate contracts, *in no jurisdiction can a party retain what it has received under such a contract and refuse to perform the contract.* Appleton v. Citizens' Central Nat. Bank of New York, 190 N. Y. 417, 83 N. E. 470, 32 L. R. A. (N. S.) 543; American Surety Co. v. Philippine Nat. Bank, 245 N. Y. 116, 156 N. E. 634, where the authorities in this state are reviewed.

"The judgment and orders below must therefore be affirmed to the extent in which they have required the defendant to return the pledged bonds *upon the repayment of the deposited money, with interest.*" (p. 754.)

In the case of *Schornick v. Butler, et al.,* ..... Ind. ....., 185 N. E. 111, decided March 28, 1933, there was under consideration the pledging of assets by a bank and the right of the receiver of the bank to hold deposits and at the same time require a return of the pledged assets. In disposing of the case the court said:

"Under the depository statute the bank might have pledged eligible bonds directly to the municipality as security for its deposits. The transaction here is no different in effect. The securities were pledged to the appellees, who, in turn, pledged themselves to secure the deposits. In either case the pledged securities were only liable to the extent of the cash actually deposited. The bank parted with an interest in the securities equal to the deposit subject to the condition that, to the extent to which it repaid the cash, it

would reclaim the securities. It amounts to no more than a sale of securities at their actual value for cash. *The general creditors of the bank lost nothing by the transaction,* and, if they are affected at all, they are benefited since the bank is more liquid by reason of having the cash rather than the securities. The appellees gained nothing. The public deposit or its proceeds was used, or will be used, for the payment of general creditors of the bank. No more than an equal amount of the pledged notes will be withheld.

"The action sounds in equity. The general creditors of the bank or the appellant, their representative, cannot be heard to say that the pledging of the securities was illegal while they retained the benefits of the transaction. Melaven v. Hunker et al., 35 N. M. 408, 299 P. 1075.

" 'It would be unconscionable to permit the general creditors to profit where they had no loss, at the expense of the appellees, who have profited nothing and have done no wrong. It must not be permitted unless there is some insuperable rule of law which requires it.

" 'Justice alone can be considered in a court of chancery, and technicalities never be tolerated except to obtain and not to destroy it.' " (p. 112.)

In the case at bar the receiver, of course, has no greater rights or powers than the banking corporation for which he is acting as receiver. *Scott v. Armstrong,* 146 U. S. 507.

The First National Bank of El Paso, Texas, while a going concern, would not have been permitted to retain

the railroad deposits and at the same time demand the return to it of the pledged assets, and so likewise the receiver Pottorff of said national bank has no greater or higher right, title or claim than the bank itself.

As said by Chief Justice White in *Fourth State National Bank v. Yardley*, 165 U. S. 653:

> "The receiver took no greater rights in the property of the insolvent bank which came into his possession than that which the insolvent bank possessed."

It is respectfully submitted that a case is not only made out for the granting of the writ of certiorari but also for a reversal of the decree of the court below.

Respectfully submitted,

CHARLES N. BURCH,
EDWARD W. SMITH,
Amici Curiae.

Emphasized words herein are those of the Amici Curiae.

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In the

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 128

THE TEXAS AND PACIFIC RAILWAY COMPANY,
Petitioner,

versus

S. O. POTTORFF, Receiver of The First National Bank of El Paso, Texas,
Respondent.

PETITION FOR REHEARING

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Dallas, Texas,
March 16, 1934.

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Respondent.

PETITION FOR REHEARING

To the Honorable the Supreme Court of the United States:

This petition for rehearing is filed pursuant to Supreme Court Rule 33, and an order of the Court enlarging the time for filing to and including March 19, 1934.

Three primary grounds are urged in support of this petition, viz.:

1. In enacting section 8 of the National Bank Act of 1864 (12 USCA § 24), Congress adopted the language of section 18 of the New York banking law which the Court of Appeals of that State in 1860 had construed to authorize the pledging of assets as security for both public and private deposits; and in adopting that language, four years after that decision, Congress likewise adopted the construction placed upon it by that Court;

2. To authorize the ratable distribution to general creditors of both the railway company's deposits, procured by the bank as a result of the pledge agreement, and the proceeds from the sale of the pledged liberty bonds, is to enforce in favor of those creditors an agreement which the Court has condemned, contrary to its announced doctrine "that no rights arise on an *ultra vires* contract".

3. Assuming the invalidity of the pledge agreement, the railway company's deposits never became subject to ratable distribution among general creditors, but were held by the bank, and later by its receiver, as special deposits in trust, and petitioner should be permitted to recover this trust fund in its second cause of action now pending in the District Court, upon identifying such funds in their original or altered form.

First Ground

The Honorable S. P. Chase, Secretary of the Treasury during the administration of President Lincoln, was largely responsible for the passage by Congress of the National Bank Act of 1864. In his report to Congress on December 9, 1861[1], Secretary Chase advocated the passage of such an act, and stated in part:

> "It is not untried theory. In the State of New York, and in one or more of the other States, it has been subjected, in its most essential parts, to the

1 Appendix to The Congressional Globe, 37th Cong., 2d sess., pp. 23-28.

> test of experiment, and has been found practicable and useful. The probabilities of success will not be diminished, but increased, by its adoption under national sanction, and for the whole country" (p. 26).

On July 11, 1862, Congressman Hooper of Massachusetts introduced a bill (No. 568) to provide a national currency,[1] which was referred to the House Committee of Ways and Means. The House took no action on this bill, and apparently it was never reported by the Committee[2]. The Secretary of the Treasury, in his report to Congress in December 1862[3], again urged the passage of a national bank act, and during that session of Congress several bills to provide a national currency were introduced, among others one by Congressman Hooper[4], and one (S. 486) by Senator Sherman[5].

In the House debate on S. 486, which became a law on February 25, 1863[6], Congressman Spaulding of New York stated:

> "The bill in all its essential features is like the free banking law of the State of New York, which has been in successful operation in that State since 1838" (37th Cong., 3d Sess., p. 1114).

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1 The Congressional Globe, 37th Cong., 2d sess., p. 3258.
2 The Congressional Globe, 37th Cong., 2d sess., pp. 3362-3.
3 Appendix to The Congressional Globe, 37th Cong., 3d sess., p. 25.
4 The Congressional Globe, 37th Cong., 3d sess., p. 226.
5 The Congressional Globe, 37th Cong., 3d sess., p. 505.
6 United States Statutes at Large, volume 12, page 665.

For comparative purposes and the Court's convenience we set out the pertinent portions of section 18 of the New York banking law of 1838 and section 11 of the National Bank Act of 1863:

New York Law of 1838.

"§ 18. Such association shall have power to carry on the business of banking, by discounting bills, notes and other evidences of debt; by receiving deposits; by buying and selling gold and silver bullion, foreign coins and bills of exchange, in the manner specified in their articles of association for the purposes authorized by this act; by loaning money on real and personal security; and by exercising such incidental powers as shall be necessary to carry on such business; * * *" (Laws of New York, 61st Session, Chapter 260, page 249).

National Act of 1863.

"Sec. 11. *And be it further enacted,* That every association formed pursuant to the provisions of this act * * * shall have power to carry on the business of banking by obtaining and issuing circulating notes in accordance with the provisions of this act; by discounting bills, notes, and other evidences of debt; by receiving deposits; by buying and selling gold and silver bullion, foreign coins, and bills of exchange; by loaning money on real and personal security, in the manner specified in their articles of association, for the purposes authorized by this act, and by exercising such incidental powers as shall be necessary to carry on such business; * * *" (United States Statutes at Large, Chapter 58, volume 12, page 668).

For some reason not readily ascertainable from the congressional records available to petitioner, the Act of February 25, 1863 was supplanted by another National Bank Act passed by Congress and approved on June 3, 1864 (13 Stat. 99, Chap. 106). Section 8 of the Act of 1864 (12 USCA § 24, par. 7) in substantial effect was a reenactment of section 11 of the Act of 1863, and, like it, followed closely the language of section 18 of the New York banking law of 1838, as shown by the following comparison:

New York Law of 1838.

"§ 18. Such association shall have power to carry on the business of banking, by discounting bills, notes and other evidences of debt; by receiving deposits; by buying and selling gold and silver bullion, foreign coins and bills of exchange, in the manner specified in their articles of association for the purposes authorized by this act; by loaning money on real and personal security; and by exercising such incidental powers as shall be necessary to carry on such business; * * *" (Laws of New York, 61st Session, Chapter 260, page 249).

National Act of 1864.

"Sec. 8. Such association shall have power to * * * exercise under this act all such incidental powers as shall be necessary to carry on the business of banking by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; by obtaining, issuing, and circulating notes according to the provisions of this act; * * *" (United States Statutes at Large, Chapter 106, volume 13, page 101).

From this legislative history it is clear that Congress substantially adopted the language of section 18 of the New York banking law of 1838 as section 11 of the National Bank Act of 1863 and as section 8 of the National Bank Act of 1864, and under the decisions[1] of this Court, Congress likewise adopted the construction theretofore placed upon that language by the Court of Appeals of the State of New York.

We must now ascertain what construction, if any, had been given to the language of section 18 of the New York banking law of 1838 by the Court of Appeals of New York prior to the passage by Congress of the National Bank Acts of 1863 and 1864. This inquiry brings us to the decision of that court in 1860 in *Smith v. Lansing, 22 New York 520, New York Court of Appeals Reports, Book V, page 370.* In that case the president of Oliver Lee & Co.'s bank gave his personal bonds, and later the bonds of himself and other co-sureties, to secure the deposit of certain state funds and also the deposits of the Western Savings Bank. To protect himself and his co-sureties, the president purchased certain real property with funds belonging to the bank, taking title in his own name. Subsequently the bank became insolvent and its receiver brought an action in the Superior Court of Buffalo to compel the bank's president

1 Cathcart et al v. Robinson, 5 Peters 264, 280, 8 L. ed. 120, 126; Panama R. Co. v. Rock, 266 U. S. 209, 212-213, 69 L. ed. 250, 252; Marlin v. Lewallen, 276 U. S. 58, 62-63, 72 L. ed. 467, 469.

to convey said real property unconditionally to him. This action necessarily involved a consideration of the power of the president to hold the real estate purchased with the bank's money as protection against liability on the deposit bonds, and in holding that this power existed under section 18 of the state banking law, the New York Court of Appeals stated in part:

> "The general banking law confers upon associations formed under it the powers, among other things, to carry on the business of banking, etc., by discounting bills, notes, and evidences of debt; by receiving deposits; by loaning money on real and personal security; and by exercising such incidental powers as shall be necessary to carry on such business; to choose one of their number as president, and to appoint such other officers and agents as their business may require, etc. (Laws of 1838, chap. 260, § 18.)" (22 New York 522).
>
> "Suppose, then, that this bank had been managed by a board of directors, and, at a regular meeting, such directors had adopted a resolution authorizing their president to apply for and receive on deposit any portion of the revenues of the State, and had authorized him to procure other persons to join with him in a bond to the State conditioned to account for and pay over the moneys so deposited; and, in pursuance of such resolution, the president had become personally liable, by a proper bond, to account and pay over, etc., and had procured others, not connected with the bank as officers or stockholders, to become jointly bound with him as obligors in such bond, and the bank had thereupon re-

ceived and used the moneys of the State: can there be any doubt that the bank would have been legally bound to indemnify and save harmless the obligors in such bond from loss or damage in consequence of their becoming parties to it? It seems to me not. And it seems equally clear that it would have been competent in such case for the bank, at any time after such bond had been given, to assign or transfer to the president, or to him and the other obligors so procured by and bound with him, any property or means in their power, sufficient for that purpose, to indemnify him or them against such bond, provided such assignment or transfer was not made in contemplation of insolvency. The same would be true, as it seems to me, if, instead of the president, with others not connected with the bank, becoming personally obligated, the directors had all united in a like personal obligation to secure the State, and had, at the same time, or afterwards, and while the bank was solvent, by resolution duly made, set apart in due form any of the assets or securities belonging to the bank, to a reasonable amount or value, for their indemnity against such personal liability. If provision could thus be made, through the action of a board of directors, for the security of depositors in a bank, and for indemnifying the sureties to such depositors, it is difficult to perceive why the same things might not be done by and through the agency of a president, clothed with powers equal to such as are possessed by a board of directors, especially in the case of a bank which has no board of directors. If the defendant, in the case at bar, had been obliged, in order to protect the other obligors in the bonds, to pay any portion of the moneys deposited by the State with the bank from his individual resources,

there could be no question of his right to take and retain, upon the first opportunity, from the cash funds of the bank sufficient to reimburse himself" (22 New York 523-524).

"I think it cannot be maintained that the plaintiff, under the facts found, is entitled to have the property in question conveyed to him, as receiver of the effects of the bank, without relieving the defendant from his liability on his bonds to the people and to the savings bank, if the bank itself would not be entitled to the same judgment, provided there had not been a receiver appointed, and on the supposition that it is now, and had always been, in successful operation as a banking association. All the transactions involved in the question under consideration took place before the failure of the bank, and at times when, for aught that appears, it was solvent and prosperous; and the receiver could acquire no claim or right, by virtue of his appointment, as against the defendant, which the association could not, at those times, have enforced against him. The defendant and his co-sureties had paid and were liable to pay, at the time of the trial, upon the three bonds to the people of this State, and the bond to the Western Savings Bank, over and above what they had received in dividends or otherwise, by way of reimbursement, an amount in the aggregate exceeding $48,000. The three parcels of real estate mentioned in the first three counts of the complaint and which is the property now in controversy, were worth, at the time of the trial, in the aggregate, the sum of $24,000. This property is all the defendant has to indemnify himself and his co-sureties for such payments and liabilities. The sureties in each of the bonds were procured by the defendant, as president and managing agent,

for the benefit of the bank; and the deposits could not have been obtained without giving security, etc. The co-sureties with the defendant became obligated with him at his request; and he is, therefore, bound to protect them. * * * It was lawful and proper that he and his co-sureties should have put into his or their hands, by the association, means for their protection and indemnity against the large liabilities which they incurred by the execution of the several bonds mentioned; and this could not be done except by the defendant's own action, as he was the only organ through and by which the association could transact that or any other business. The association have received the direct benefit of the several amounts of money to secure which the bonds were given, and the creditors have indirectly had the benefit of the same by the consequent increase of the assets of the association. The defendant acquired title in his own name to the several parcels of real estate, and continues to hold the same, for the purpose of securing himself and his co-sureties from and against their liability on the several bonds referred to. Upon these facts—all of which are either stated in the complaint or found by the judge before whom the cause was tried—a strong equity in favor of the defendant is presented. He has the legal estate in the lands in question, and the plaintiff comes with an appeal to the equitable powers of the court, and asks to have the defendant divested of such legal estate and have it vested in himself unconditionally for the benefit of the creditors of the association, which, with such creditors, have, directly and indirectly, enjoyed the fruits of the transactions out of which the claim of the plaintiff, their representative, arose.

"If this is equity, it must be by reason of the stern, unbending character and extended application of the principle before referred to. That principle, in its proper, just and equitable application, I am ready to stand by and enforce. But I do not believe it requires the sacrifice of substance to form, nor the prostration of plain and manifest justice, under the guise of equity or public policy" (22 New York 525-527).

"But I am not willing to rest my conclusion on the grounds just stated. No wrong has been done by the defendant. Neither the association nor its creditors have been injured by him. As heretofore remarked, he stood in the place of a board of directors, with all the powers which the shareholders were able to delegate to him, which were no less than all they themselves possessed, so far as respected the corporate transactions of the association. It was not only lawful for him to apply for and receive the moneys in question, but his duty to do so, if he supposed they could be used to advantage in the business of the association. These moneys could not be obtained without security beyond the corporate responsibility of the association. He was, then, bound to furnish such security, if in his power; and, in doing so, it was lawful for him to pledge the property of the association to indemnify the sureties. It would have been lawful, if the canal board and savings bank would have been satisfied with it, for him to have given his own individual bonds, without any other sureties, and to have taken a like pledge for his own individual indemnity. But he procured others to unite with him in the bonds. He had, therefore, a direct interest and a clear right to indemnify himself and his co-sureties, through the property and means of

the association, against his and their liabilities so incurred. * * * To secure indemnity against these liabilities was a duty the defendant owed, not only to himself, but pre-eminently to the sureties whom he had procured to be bound with him" (22 New York 528-529).

"*Comstock, Ch. J.* (concurring):

"The plaintiff in this case, representing, as receiver, no greater rights than the bank would have if it were a party to this controversy, demands from the defendant a conveyance of the titles acquired in the manner stated, and, in support of that demand, he invokes the doctrine that an agent or trustee cannot purchase, for his own benefit, an estate to which the agency or trust relates. The general doctrine is extremely familiar. * * * But when we come to take a more exact view of the actual circumstances of the case, I see no room for the application of the rule invoked or any of its analogies. * * * It appears that the defendant purchased the lands using the funds of the bank, and took the title to himself, with the intention of holding it for the indemnity of himself and others who had united with him in becoming security to the State, and to a savings bank in Buffalo, for moneys deposited with the institution. The finding at the trial is, that the defendant took title to the several parcels of land, claiming to hold them for that purpose. The transactions, in their real character, amounted, therefore, to an appropriation by the financial head of the bank of a certain portion of its funds and assets for the purpose of securing himself and his associates for the liabilities they had assumed. If he had a right to take a pledge for that purpose, it can make no difference in what

form he kept the value in pledge. He might keep the assets thus appropriated, or he might invest them in land. If the bank might complain of such investment as unauthorized or unwise and might, on that ground, charge him with a loss, if one should occur, this would furnish no reason for taking the value thus appropriated, out of his hands unconditionally, provided he had a right to secure himself and his associates by taking any pledge whatever. * * * The only question, then, is, whether he and his associates, in the liability which they had assumed, had a right to be secured by his act in the premises. And I think they had this right. It is in the usual line of business for a bank to take deposits. The State, as we know, requires security to be given, *and any other depositor may require it.* And if the president or cashier, being the general agent or manager, enters into the required bonds and procures others to unite with him, I see no reason why he may not, in good faith, take a counter security from the institution. He may be the actor in his official capacity, and, with others united in interest, he may also be the recipient in the transaction. What is fairly done for such a purpose should be allowed to stand. The result in this case will violate no rule of law while equity will be promoted" (22 New York 531-534).

The foregoing excerpts from the opinion in the Lansing case show the court based its decision upon the proposition that the power to pledge assets to procure deposits was a power incidental to the express power to receive deposits under section 18 of the New York

law, and when Congress adopted the language of that section it must have intended to confer a similar power upon national banks under the Act of 1864.

Petitioner is conversant with the opinion in *State Bank of Commerce of Brockport v. Stone, 184 N. E. 750,* but that decision, rendered 69 years after Congress adopted the New York law, cannot defeat the well-recognized principle of law that the construction placed upon an act, before its adoption, by the highest court of the state, is carried into that act when adopted by another legislative body.[1]

In the case at bar the railway company never agreed to place its moneys on deposit without security and from the opening of its account until January 29, 1931 they were secured by corporate surety bonds on which the bank paid the premiums. Unknown to the railway company, but known to the officers of the bank, one of the surety companies was threatening cancellation of its bond and it was extremely doubtful that another surety company could be procured to assume the risk. The bank wished to retain the railway company's deposits, amounting to an average daily balance of approximately $50,000, but knew they would be withdrawn if the surety bonds were canceled. To avoid this and obtain future deposits, the pledge of liberty bonds was given, and on the faith of that pledge additional deposits were

1 Panama R. Co. v. Rock, 266 U. S. 209, 212-213, 69 L. ed. 250.

made. Clearly the Court of Appeals of New York had this kind of a case in mind when writing its opinion in the Lansing case, and undoubtedly Congress had it in mind when adopting the New York law.

If there be any merit in respondent's arguments *in terrorem* all dangers can readily be eliminated by the passage of an amendatory act during the present session of Congress, which would not divest this Company of its property rights established upon the true meaning of the Act of 1864. In this connection we think pertinent the following excerpt from the opinion of the Court in *National Bank of Genesee v. Whitney, 103 U. S. 102, 26 L. ed. 444:*

> "Judicial decisions affecting the business interests of the country should not be disturbed except for the most cogent reasons, certainly not because of subsequent doubt as to their soundness. The prosperity of a commercial community depends, in a great degree, upon the stability of the rules by which its transactions are governed. If there should be a change, the Legislature can make it with infinitely less derangement of the interests of the country than would follow a new ruling of the court, for statutory regulations would operate only in the future."

Second and Third Grounds

The deposits of the railway company which the receiver will distribute to general creditors were procured

by the bank as a result of the pledge agreement, and to permit such distribution of those deposits while refusing to enforce the pledge through which they were procured, is to enforce the rights of general creditors arising on a contract declared *ultra vires*, contrary to the announced doctrine of the Court that "no rights arise on an *ultra vires* contract, even though the contract has been performed".

To relegate the railway company to a mere action on an implied contract and to restrict its right to recovery to the status of other general creditors would not afford the relief to which it is entitled under the facts of this case. In such event the general creditors would receive the full benefit of the contract of deposit while the rights of the railway company under that agreement are denied. As stated by this Court in several decisions[1], the rule that a party may recover moneys parted with under an *ultra vires* contract was promulgated for the purpose of absolutely destroying such contract, which would not be the case if either party thereto were permitted to retain the benefits of it. This rule of course would be defeated under the present decision of the Court in those cases where insolvency has intervend even though it be shown that the actual benefits passed

1 Central Transportation Co. v. Pullman's Car Co., 139 U. S. 24, 60, 35 L. ed. 55, 60; Pullman's Palace Car Co. v. Central Transportation Co., 171 U. S. 138, 43 L. ed. 108; Aldrich v. Chemical National Bank, 176 U. S. 618, 44 L. ed. 611.

into the hands of the receiver and are about to be distributed by him to general creditors. If a party to an *ultra vires* contract is entitled to recover money with which it has parted as a result of such contract it certainly should be permitted to recover it from any person into whose hands it may have passed whether that person be a receiver or any other party acting in a fiduciary capacity.

Moreover, the circumstances under which the bank received the railway company's deposits, if the pledge agreement be invalid, give rise to a constructive trust. Unknown to the railway company but known to the officers of the bank, one of the real reasons for substituting a pledge of liberty bonds in lieu of corporate surety bonds was the threat of one of the surety companies to cancel its bond and the inability of the bank to procure another surety company to assume the risk. The bank's officers withheld this information from the railway company and predicated their request for the substitution solely upon the ground that the bank wished to save the bond premiums which it had been paying. This false representation in inducing the railway company to accept the pledge in lieu of the surety bonds, and to make further deposits on the faith of that pledge, was a circumstance of special misconduct and it is difficult to perceive how it can be held that deposits thereafter made by the railway company in reliance upon

such pledge agreement, now declared invalid, became general assets of the bank, subject to ratable distribution to general creditors in the event of insolvency. This is not a case like *Blakey v. Brinson, 286 U. S. 254, 76 L. ed. 1089.* The decision in that case rests squarely upon the proposition that no trust was created because the depositor by agreement became a general creditor of the bank and his deposits became general assets of the bank as a result of that agreement. In the case at bar the railway company never agreed to become a general creditor of the bank nor that its deposits should become general assets of the bank if they in fact were not secured; and, the pledge agreement being invalid, petitioner's deposits were held by the bank, and later by its receiver, as special deposits in trust for the railway company.

When the bank failed the railway company had $54,646.94 on deposit and when the receiver took charge there was $113,686.92[1] in actual cash in the bank's vaults, and there was due it from other banks in the United States, less overdrafts, the sum of $939,903.15[1]. It is certain that the bank's assets were increased by the railway company's deposits; it is also certain that

1 First report of Receiver S. O. Pottorff to the Comptroller of the Currency, Trust No. 1720, on file in the Comptroller's office.

there came into the possession of the receiver a sum of money greatly in excess of those deposits; and in order to do equity[2] an equitable lien should be fixed upon the property in the receiver's hands or the Court should permit the railway company to recover from the receiver, in petitioner's second action now pending in the District Court, the deposits which the receiver holds in trust, upon proof that those deposits came into his possession in their original or altered form.

Conclusion

Wherefore, petitioner respectfully prays that this petition for rehearing be granted; that the decree and judgment of the District Court and the Circuit Court of Appeals for the Fifth Circuit be reversed and the cause remanded with direction to grant the relief sought by petitioner; or, in the alternative, if those decrees and judgments be affirmed, that such action be without prejudice to petitioner's right to prosecute its second cause of action, now pending in the District Court, against the receiver to recover the deposits which he

2 Central Transportation Co. v. Pullman's Car Co., 139 U. S. 24, 60, 35 L. ed. 55, 60; Pullman's Palace Car Co. v. Central Transportation Co., 171 U. S. 138, 43 L. ed. 108; Aldrich v. Chemical National Bank, 176 U. S. 618, 44 L. ed. 611; Citizens' Central Natl. Bank v. Appleton, 216 U. S. 196, 54 L. ed. 443.

holds in trust or to fix an equitable lien upon the property in his possession.

Dated at Dallas, Texas, March 16, 1934.

Respectfully submitted,

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Certificate of Counsel

I, M. E. Clinton, of counsel for petitioner, do hereby certify that the foregoing petition for rehearing is presented in good faith and not for delay.

(Signed) M. E. CLINTON,
Of Counsel for Petitioner.

SUPREME COURT OF THE UNITED STATES.

No. 128.—October Term, 1933.

The Texas & Pacific Railway Co., *vs.* S. O. Pottorff, Receiver of the First National Bank of El Paso.	On Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

[February 5, 1934.]

Mr. Justice Brandeis delivered the opinion of the Court.

The main question for decision is whether a national bank has power to pledge a part of its assets to secure a private deposit.

The First National Bank of El Paso, Texas, failed on September 4, 1931, and S. O. Pottorff was appointed receiver. The Texas & Pacific Railway Company was then, and long had been, a depositor. To secure it as such the bank had, in January, 1931, pledged $50,000 Liberty Bonds and held them for the Railway in the Trust Department of the bank. The balance in the Railway's regular checking account at the time of the failure was $54,646.94. Of this claim it made proof as a secured creditor. The receiver approved the amount of the claim, but denied the validity of the pledge; and he tendered a dividend check only for the amount to which the Railway would have been entitled as an unsecured creditor. Thereupon, the Railway brought, in the federal court for western Texas, this suit against the receiver, praying, in the alternative, that the bonds be delivered to it; or that they be sold for its benefit; or that the claim be paid in full with interest. The receiver filed a cross-bill praying that the bank's title to the bonds be quieted.

The case was first heard upon motions to dismiss the bill and the cross-bill. The decision on the motions was postponed until after hearing the case upon the evidence. Thereupon the court dismissed the bill and entered a decree for the receiver upon the cross-bill,

holding that the pledge was void and that the Liberty Bonds constituted assets to be administered for the benefit of the general creditors of the bank. The Circuit Court of Appeals affirmed the decree. 63 F. (2d) 2. This Court granted certiorari. 290 U. S. —. The Railway contends that the bank had power to make the pledge; that even if the bank did not have such power, the receiver is not in a position to question the validity of the pledge; and that even if he is not estopped from doing so, he may not disaffirm it without returning the consideration therefor received by the bank. We are of opinion that none of these contentions is sound.

The District Court found the following additional facts. The relation between the Railway and the bank began in 1922 when the Railway was in receivership. Then, an order was entered appointing the bank a depositary upon condition that it should furnish a bond with solvent sureties. An acceptable bond was then given in the sum of $25,000. When, in 1924, the receivership terminated, the Railway continued its deposit account; and a bond in like amount was given with the National Surety Company as surety. When, in 1927, the average deposits had increased to about $50,000, an additional bond of $25,000 was given with the Maryland Casualty Company as surety. While these bonds were in full force and effect and the bank was solvent, it requested the Railway to accept, in substitution for the surety bonds, the pledge of the $50,000 Liberty Bonds, giving as its reason for the request that the premiums payable on the surety bonds were a burden from which it wished to be relieved. The Railway expressed willingness to assent to the substitution, but only on condition that thereby it would be as fully protected as by the surety bonds. The bank and its attorney gave this assurance; and thereupon the pledge was substituted for the surety bonds and these were cancelled. Without that assurance, the Railway would not have consented to the cancellation of the surety bonds; or if they had been cancelled without its consent, would have immediately withdrawn all of its deposits. In reliance upon the assurances and the pledge, the Railway continued until the failure to make deposits; and in fact increased its deposits.

National bank examiners commenced on August 6, 1931, an examination of the bank. Within a few days, they learned from the bank's books that the pledge had been made; but neither the

examiners nor the Comptroller of the Currency advised the bank's officers that the pledge was beyond the powers of the bank or that it was irregular or otherwise objectionable. The bank had frequently secured private deposits by surety bonds; but never before by a pledge of assets. The examiners concluded their investigation on August 20, 1931. The failure occurred on September 4, 1931.

First. National banks lack power to pledge their assets to secure a private deposit. The measure of their powers is the statutory grant; and powers not conferred by Congress are denied.[1] For the Act[2] under which national banks are organized constitutes a complete system for their government, *Cook County National Bank* v. *United States*, 107 U. S. 445, 448; *California Bank* v. *Kennedy*, 167 U. S. 362, 366; *First National Bank* v. *Missouri*, 263 U. S. 640. Confessedly the power to pledge assets to secure a private deposit was not granted in specific terms. The contention is that this power is incidental to the general grant of powers "necessary to carry on the business of banking . . . . by receiving deposits;" and, hence, is implied.[3]

There is no basis for the claim that the power to pledge assets is necessary to deposit banking. The record is barren of evidence that the practice of so pledging assets has ever prevailed among national banks. And facts of which we take judicial notice indicate that among national banks such action must have been deemed contrary to good banking practice.[4] From the establishment of

[1]First National Bank *v.* National Exchange Bank, 92 U. S. 122, 128; Logan County Bank *v.* Townsend, 139 U. S. 67, 73. California National Bank *v.* Kennedy, 167 U. S. 362; Concord First National Bank *v.* Hawkins, 174 U. S. 364; First National Bank *v.* Converse, 200 U. S. 425, 439. Compare McCormick *v.* Market Bank, 165 U. S. 538, 549; Merchants National Bank *v.* Wehrman, 202 U. S. 295.

United States *v.* Robertson, 5 Peters 641, and Planter's Bank *v.* Sharp, 6 How. 300, have no application to the National Banking Act.

[2]Act of June 3, 1864, c. 106, § 8, 13 Stat. 101; R. S. 5136; 12 U. S. C. § 24, Seventh.

[3]Compare Jacob Ruppert *v.* Caffrey, 251 U. S. 264, 301.

[4]No mention of securing a private deposit in a national bank by a pledge of assets or otherwise has been found in any published report of the Comptroller (compare note 6); or in any of the 52 available treatises or textbooks on banks and banking practice published since 1900; in any of the annual proceedings of the American Bankers Association or in any issue of the American Banker's Journal; or in any issue of The Commercial and Financial Chronicle since 1900; or in the New York Times Index since 1913. Compare "Contemporary Banking", by Willis, Chapman & Robey (1933), p. 336.

the system in 1864 to March 1, 1933, 2159 national banks failed[5] and there has been much litigation arising from their insolvency; but only two other reported cases have been found involving a pledge of assets to secure a private deposit, and in those cases, very recent ones, the existence of the power was denied.[6] *Smith* v. *Baltimore & O. R. Co.*, 48 F. (2d) 861; 56 F. (2d) 799; *Illinois Central R. Co.* v. *Rawlings*, 66 F. (2d) 146. In the case at bar, there is a specific finding that the transaction challenged was the only instance in which this bank had ever pledged assets to secure a private deposit. Surely action cannot be deemed a necessary incident of a business when only a single instance has been found in which it was taken. Moreover, even a practice commonly pursued may not be a necessary one.[7]

To permit the pledge would be inconsistent with many provisions of the National Bank Act which are designed to ensure, in case of disaster, uniformity in the treatment of depositors and a ratable distribution of assets. Compare *Davis* v. *Elmira Savings Bank*, 161 U. S. 275, 290. This policy of equal treatment was held to preclude, in case of a national bank, even the preference under § 3466 of the Revised Statutes which otherwise is accorded to the United States when its debtor becomes insolvent. *Cook County National Bank* v. *United States*, 107 U. S. 445. The effect of a pledge is to withdraw for the benefit of one depositor part of the fund to which all look for protection. Thereby the legitimate expectations of a great body of the depositors are defeated and confidence in the fairness of the national banking laws and ad-

[5]Annual Report of Comptroller of the Currency (1932) 148. Federal Reserve Bulletin (1933) 144. (Figures from these two sources have been combined.)

[6]In that case the parties stipulated, and the District Court found (p. 864) that "during, before, and after the said period of February 23, 1928, to July 31, 1930, when the said Comptroller was requested by national banks or others for an opinion upon the power of national banks to pledge securities to secure a private depositor, in every instance the Comptroller disapproved of such pledges by stating that in his opinion national banks had no such power."

[7]Compare Federal Reserve Bank *v.* Malloy, 264 U. S. 160, 167. A practice is not within the incidental powers of a corporation merely because it is convenient in the performance of an express power. Merrill *v.* Monticello, 138 U. S. 673, 692; compare Beaty *v.* Knowles, 4 Peters 152, 168-171.

ministration is impaired. It is no answer to say that the other depositors are benefited by the increased resources which the pledge brings to the bank, or at least are not harmed, since the new funds take the place of the securities pledged and are available to meet liabilities.[8] The immediate safety of unsecured creditors depends on the bank remaining open and solvent; the pledge reduces the fund of quick assets available to meet unusual demands without any assurance that the deposit will be used to replenish this fund.

The fact that this bank had frequently secured private deposits by surety bonds lends no support to the contention that the power to pledge assets is necessary to carrying on the business of deposit banking. Such a practice would likewise be a departure from the policy of equal treatment of depositors; but the loss to other depositors resulting from such action would be far less serious. A pledge withdraws capital assets, while the giving of a surety bond merely increases the bank's expenses. There is, however, no finding that among national banks there exists the practice of securing by surety bonds some private deposits. If there has been such a practice, it must have been a secret one; for reference to it has not been found in either official reports, or the books on

[8] These arguments seem to ignore the realities of the banking business. The primary interest of a depositor is that the bank shall be able to pay as and when he demands payment. The ability to do so depends not on the bulk of the assets but on their liquidity. The law applicable to national banks requires them to maintain as reserves in the form of cash or of cash balances with a federal reserve bank, fixed percentages of their demand deposits in order to assure ability to meet probable demands as they arise; but such reserve is commonly deemed insufficient to meet possible emergencies. Because of this, soundly managed banks maintain so-called "secondary reserves", usually in the form of government obligations which can be liquidated quickly with little or no loss. The effect of pledging quick assets for particular deposits is to reduce the fund available for meeting current demands of an unexpected nature. The funds received from the deposit are not necessarily an equivalent for the securities withdrawn from available resources. In the first place the deposit, in the process of clearing and collection, may serve merely to cancel liabilities against the bank. This may mean that there will be fewer competing claims in case of insolvency, but it will still be true that the reserves have been depleted considerably beyond what would be justified by reason of the cancellation of the liability. In the second place, to the extent that the deposit represents free funds, it is not probable that the deposit will be used to buy other low yield quick assets to take the place of those which have been pledged.

banking or other publications dealing with financial affairs.[9] Whether a national bank could legally engage in such a practice we have no occasion to decide.[10]

The Railway insists that Congress in providing that the Secretary of the Treasury might deposit public money in national banks upon receiving satisfactory security by "the deposit of United States bonds or otherwise," Act of June 3, 1864, c. 106, § 45; 13 Stat. 113[11] assumed a general power in national banks to pledge their assets to secure deposits; and that the assumption indicates that it intended this power to be among the "incidental" powers granted by section 8. But without such assumption, the duty of the Secretary to demand a pledge authorizes a national bank to make it.[12] We may not import into section 8 a meaning not de-

[9]See note 4. However, compare Lunt, Surety Bonds (1930), 206.

[10]Nebraska *v.* First National Bank of Orleans, 88 Fed. 947, and Interstate National Bank *v.* Ferguson, 48 Kan. 732, held in the case of a deposit of public funds that the practice was legal. Two Attorneys General have expressed the opinion that national banks lacked the power to pay for guaranteeing all depositors. 27 Op. Att'y Gen. 37, 40; 272, 279. But see 30 Op. Att'y Gen. 341, *contra.*

[11]The original national bank act of 1863 had provided merely that the Secretary of the Treasury might deposit public moneys in national banks. By legislation subsequent to 1864 national banks have been made depositaries of moneys of bankrupt estates, Act of July 1, 1898, c. 541, § 61, 30 Stat. 562; of Indian moneys, March 3, 1911, c. 210, § 17, 36 Stat. 1070; May 25, 1918, c. 86, § 28, 40 Stat. 591; of funds in the hands of the receivers of insolvent national banks, May 15, 1916, c. 121, 39 Stat. 121; of postal funds, May 18, 1916, c. 126, § 2, 39 Stat. 159; of proceeds from the sale of bonds, Sept. 24, 1917, c. 56, § 8, 40 Stat. 291; April 4, 1918, c. 44, § 5, 40 Stat. 504; July 9, 1918, c. 142, § 4, 40 Stat. 845; and of a number of other public funds. In all of these statutes the depositor is required to take security; but therein likewise nothing is said as to the power of the bank to pledge the required securities. Two of these statutes, those relating to deposits of the funds of insolvent banks and of bankrupt estates, have reference to the deposit of private funds. In some of the legislation, not only national, but state, banks also are made depositaries. It is true that Congress cannot make valid a pledge by a state bank, but that does not make it any the less likely that Congress intended to make valid every pledge by a national bank that would be called for under the statute. It would be the duty of a public officer depositing in a state bank to make sure that it had the power to give the security required by Congress.

[12]Where a statute specifically forbids a preferential pledge, it has been held that a public officer's duty to demand a pledge impliedly gives power to pledge in that specific case. Maryland Casualty Co. *v.* Bd. of Com'rs, 128 Okla. 58; 31 Op. Att'y Gen. (U. S.) 41.

rivable from the words of that section and inconsistent with other provisions of the Act. Moreover, if the Railway's argument were sound it would have been unnecessary to amend § 45 as was done by the Act of June 25, 1930, c. 604, 46 Stat. 809, which provides:

"Any association may, upon the deposit with it of public money of a State or any political subdivision thereof, give security for the safe-keeping and prompt payment of the money so deposited, of the same kind as is authorized by the law of the State in which such association is located in the case of other banking institutions in the State."

This amendment indicates that Congress believed that the original Act had not granted general power to pledge assets to secure deposits.[13] The fact that the amendment was made to section 45 indicates that the power to pledge was granted only as an incident of the public officer's duty to demand a pledge. If, as is suggested, the 1930 amendment was passed merely in order to settle doubts as to the power of a national bank to pledge its assets to secure deposits, the amendment would naturally have been made not to section 45, but to section 8, which contains the grant of "incidental" powers.

The Railway urges also that since the relation of the bank to its depositors is that of debtor to creditor, and since a national bank may borrow money, *Aldrich* v. *Chemical National Bank*, 176 U. S. 618; *Auten* v. *United States*, 174 U. S. 125, and pledge its assets therefor, *Wyman* v. *Wallace*, 201 U. S. 230, it may likewise pledge assets to secure a private deposit. The fallacy of this contention has been many times exposed.[14] The difference between deposits and loans is fundamental and far reaching. The amount of the deposits is commonly accepted as a measure of the bank's success; an increase of deposits as evidence of increased prosperity. The depositor does not think of himself as lending money to the bank. The modern deposit grew out of the older form of deposit in which

[13]Senator Thomas, in introducing the bill, stated in the Senate: "It is a bill simply to confer on a national bank the same opportunity for the giving of security for the safe-keeping and prompt payment of state and county moneys, as is authorized with reference to state banking institutions." 72 Cong. R. 6243.

[14]Farmers & Merchants Bank v. Consolidated School District, 174 Minn. 286, 291; State Bank of Commerce v. Stone, 261 N. Y. 175; Divide County v. Baird, 55 N. D. 45, 52; Commercial Banking & Trust Co. v. Citizen's Trust and Guaranty Co., 153 Ky. 566, 574; 27 Colum. Law Rev. 88; 79 U. of Penn Law Rev. 608, 614.

the fund was held separate and intact, and the sole purpose of the deposit was safe-keeping. Safe-keeping is still a very important function of deposit banking; and from the point of view of most depositors the chief one.[15] Borrowing by a bank (as distinguished from a re-discount) is commonly regarded as evidence of weakness.[16] Often the loan is made in the hope of averting insolvency. Loans made by one bank to another commonly involve a pledge of assets, since only upon such a condition is the transaction possible. *Wyman* v. *Wallace, supra.*

Second. The receiver is not estopped to deny the validity of the pledge. The Railway's argument is that the bank could not set up the defence of *ultra vires* since it had the benefit of the transaction; and that the receiver, as its representative, can have no greater right. Neither branch of the argument is well founded. The bank itself could have set aside this transaction. It is the settled doctrine of this Court that no rights arise on an *ultra vires* contract, even though the contract has been performed; and that this conclusion cannot be circumvented by erecting an estoppel which would prevent challenging the legality of a power exercised. *California Bank* v. *Kennedy*, 167 U. S. 362; *McCormick* v. *Market Bank*, 165 U. S. 538; *Central Transportation Co.* v. *Pullman's etc. Co.*, 139 U. S. 24.[17] But even if the bank would have

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[15]To insure fulfilment of this function the government subjects national banks to close and constant supervision so as to maintain the solvency of the bank. It is made a crime to accept a deposit with knowledge of insolvency. Only when the bank's condition measures up to the prescribed standards of safety and liquidity may deposits be received.

Though large deposits frequently represent loans by the bank to the depositor, this is less likely to be true of small accounts. Out of 30,556,105 accounts reported by 5,500 licensed member banks of the Federal Reserve System, 29,482,384 were under $2,500 and the average size of these accounts was $189. Federal Reserve Bulletin, July 1933, p. 454.

[16]The Comptroller of the Currency has insisted on the distinction between deposits and borrowings and has stated that to list borrowings as deposits—e. g., as certificates of deposit—is a grave misrepresentation of the condition of the bank. Annual Report 1890, p. 13; 1892, p. 39.

"The fact that more than one-half of the national banks reporting were not borrowing from any source is additional evidence of the stability of the national banking system." Annual Report of Comptroller of the Currency (1922), p. 26.

[17]See also Pearce *v.* R. R. Co., 21 How. 441; Thomas *v.* R. R. Co., 101 U. S. 71; Penn Co. *v.* St. Louis, etc. Ry. Co., 118 U. S. 290; Oregon Ry. Co. *v.*

been estopped from asserting lack of power, its receiver would be free to challenge the validity of the pledge. The unauthorized pledge reduced the assets available to the general creditors. It is the duty of the receiver of an insolvent corporation to take steps to set aside transactions which fraudulently or illegally reduce the assets available for the general creditors, even though the corporation itself was not in a position to do so.[18]

Third. The receiver may assert the invalidity of the pledge without making restitution by paying the pledgee's claim in full. The Railway's argument to the contrary is that when as a result of an *ultra vires* contract one of the parties is enriched at the expense of the other, the law creates an obligation to repay *ex aequo et bono* to the extent of the enrichment. The argument if applicable would not help the Railway. Such claim under the doctrine of unjust enrichment is assimilated to an obligation of contract; and does not, in the absence of an identifiable *res*[19] and a constructive trust based on special circumstances of misconduct, confer a preference over other creditors. The pledge here challenged having failed because illegal, the Railway is entitled only to a dividend as a general creditor.[20] Its right thereto is conceded.

Affirmed.

Oregonian Ry. Co., 130 U. S. 1; Concord First Nat. Bank *v.* Hawkins, 174 U. S. 364; De La Vergne Co. *v.* German Savings Inst., 175 U. S. 40.

And on the matter of estoppel in pledge cases, see authorities cited in note 14. Also Smith *v.* Baltimore & Ohio R. Co., 48 F. (2d) 861, 869; affirmed 56 F. (2d) 799; *contra:* State Bank of Commerce *v.* Stone, 261 N. Y. 175. Also compare West Penn Chemical & Mfg. Co. *v.* Prentice, 236 Fed. 891.

[18]King *v.* Pomeroy, 121 Fed. 287; Hamor v. Taylor-Rice Engineering Co., 84 Fed. 392, 399; In re O'Gara & Maguire, Inc., 259 Fed. 935, 936; In re K-T Sandwich Shoppe, 34 F. (2d) 962, 963; Shooter's Island Shipyard Co. *v.* Standard Shipbuilding Corp., 293 Fed. 706.

[19]The claimant has the burden of identifying the property in its original or altered form. Schuyler *v.* Littlefield, 232 U. S. 707. It is not enough to show that at the time of receipt the general assets of the insolvent were increased or that debts were discharged. Wuerpel *v.* Trust Co., 238 Fed. 269, 272-3; Knauth *v.* Knight, 255 Fed. 677; State Bank of Winfield *v.* Alva Security Bank, 232 Fed. 847; In re See, 209 Fed. 172; In re Dorr, 196 Fed. 292; City Bank *v.* Blackmore, 75 Fed. 771; compare Railway *v.* Spiller, 274 U. S. 304, 311; Cunningham *v.* Brown, 265 U. S. 1.

[20]Compare Blakey *v.* Brinson, 286 U. S. 254; Handelsman *v.* Chicago Fuel Co., 6 F. (2d) 163.